

**CONCURRENT RESOLUTION ON THE  
BUDGET FISCAL YEAR 2017**

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**HEARINGS**

BEFORE THE

**COMMITTEE ON THE BUDGET  
UNITED STATES SENATE**

ONE HUNDRED FOURTEENTH CONGRESS

SECOND SESSION

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**February 3, 2016—SPENDING ON UNAUTHORIZED PROGRAMS**

**April 6, 2016—BUDGETING BLIND: THE UNRELIABILITY OF FEDERAL  
FINANCIAL DATA**

**April 13, 2016—BUDGETING FOR OUTCOMES TO MAXIMIZE  
TAXPAYER VALUE**

**April 20, 2016—TAP DANCING ON THE RAZOR'S EDGE: RESTORING  
STABILITY TO GOVERNMENT OPERATIONS**

**April 27, 2016—BETTER BUDGETS, BETTER RESULTS**

**September 14, 2016—OVERSIGHT OF THE CONGRESSIONAL BUDGET  
OFFICE**



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## SPENDING ON UNAUTHORIZED PROGRAMS

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WEDNESDAY, FEBRUARY 3, 2016

U.S. SENATE,  
COMMITTEE ON THE BUDGET,  
*Washington, D.C.*

The Committee met, pursuant to notice, at 10:00 a.m., in Room SD-608, Dirksen Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Ayotte, Perdue, Whitehouse, Kaine, and King.

Staff Present: Eric Ueland, Republican Staff Director; for the Minority: Joshua Smith, Budget Policy Director.

### OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. I will go ahead and call this hearing to order. Good morning, and welcome to all that are here.

We are here today to talk about what I view as a fundamental breakdown in America's budget process, and it is a breakdown that has significant ramifications for not only Government but for our Nation. I mentioned a lot last year that we had 260 expired authorizations that we were still spending money on to the tune of \$293.5 billion. I evidently mentioned it enough that we changed that from 260 down to 256. But we increased the spending from \$293 billion to \$310 billion. We need to be going back and looking at things and making sure that we know what we are spending our money on.

It is essential to start with a premise of good government that we should authorize programs and activities before we fund them, and as the former Chairman of the Health, Education, Labor, and Pensions Committee, I strongly value the process by which programs are authorized and reauthorized. When Congress utilizes an authorization, it is creating a Federal solution to a perceived need. But over time, needs change, program flaws become apparent, technology evolves. And over time, inevitably Congress creates more programs, many of which are duplicative of existing programs, as the Comptroller General of the Government Accountability Office testified before this Committee last year.

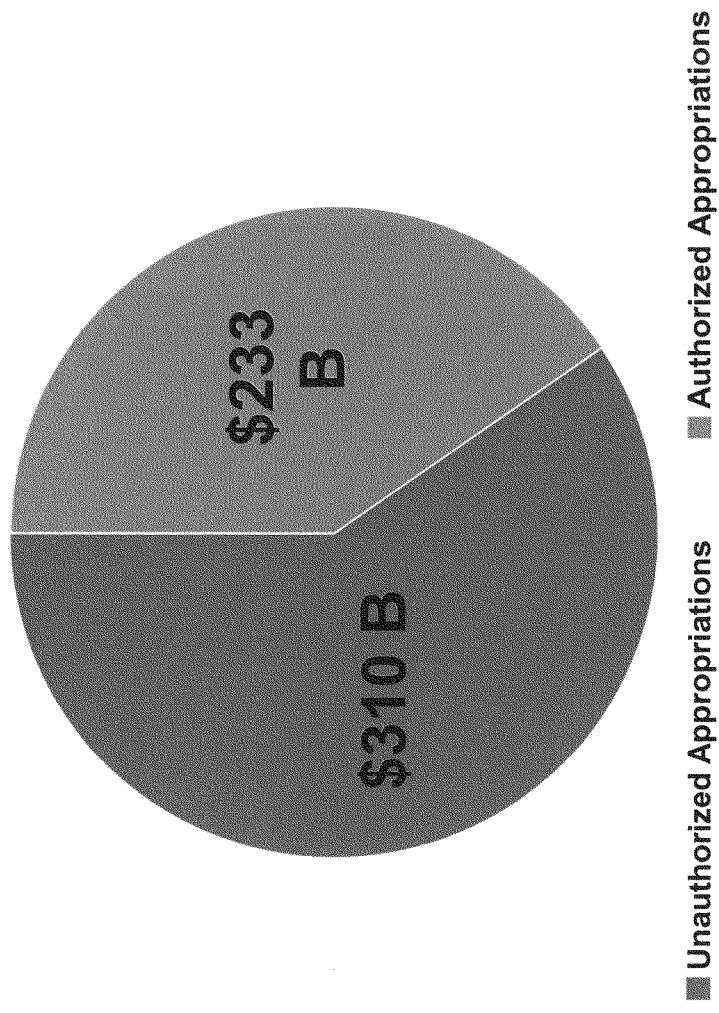
Congress must reexamine what we are actually funding in order to improve or eliminate Government programs not delivering results. By taking a closer look at these programs and activities, we would have more funding flexibility to boost important programs and priorities. This is also probably the best way to avoid creating new programs that duplicate those already being funded.

In short, there are a slew of reasons why Congress needs to periodically review and reauthorize the very Federal programs and activities it initiates. But the problem is we are not doing it.

Most of the big-ticket Federal entitlement programs like Medicare and Medicaid have permanent authorizations. Not surprisingly, they have proven to be particularly difficult to reform.

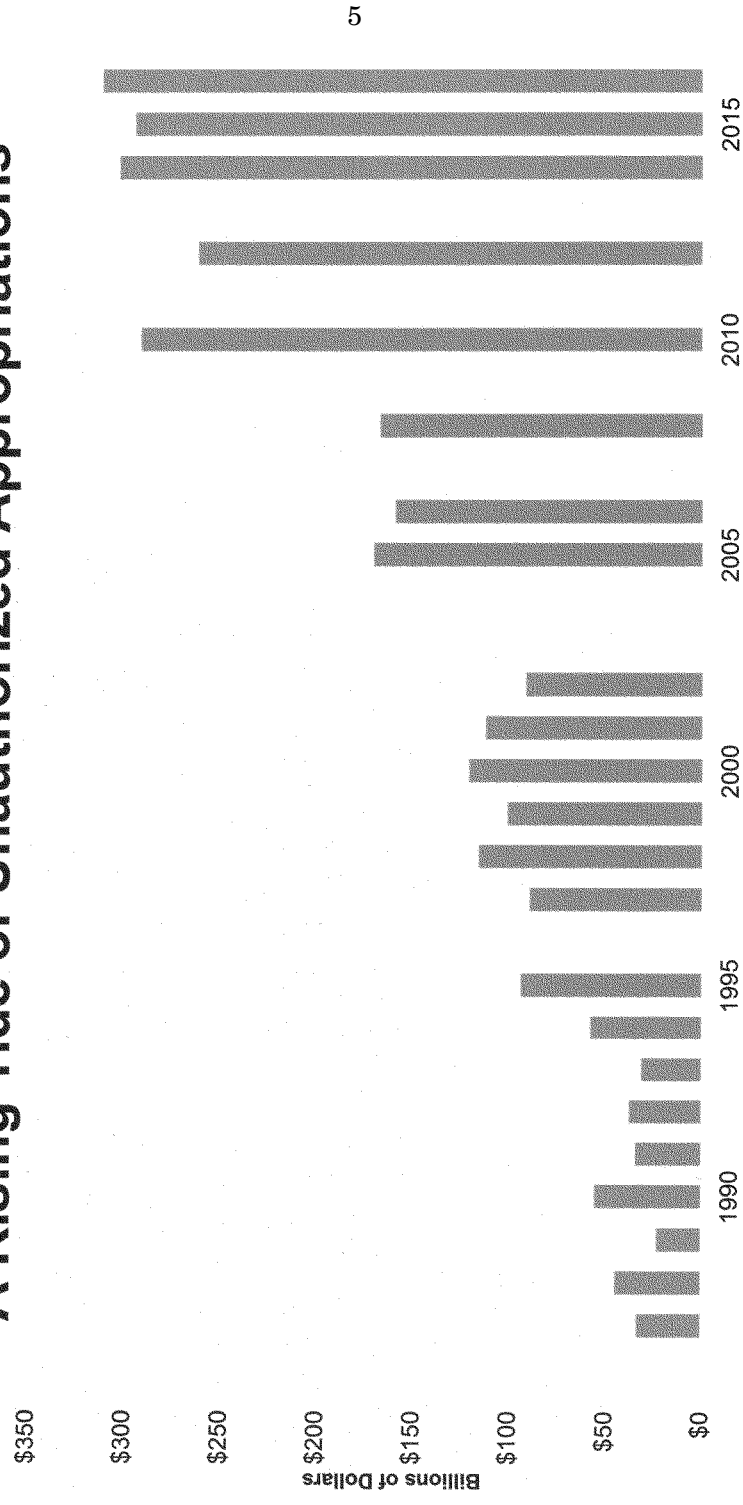
On the discretionary side, defense authorization is reauthorized annually like clockwork via the National Defense Authorization Act. But the majority of nondefense discretionary spending is now unauthorized. We have a chart showing that last year, \$310 billion of the roughly \$543 billion in nondefense discretionary appropriations went to unauthorized programs and activities. Why are we spending less on the authorized ones than we are on the unauthorized ones?

## MOST Non-Defense Disc \$ Unauthorized (FY 16)



We did not get there overnight. We have another chart using data compiled by the Congressional Budget Office showing that spending on unauthorized appropriations has been increasing over the course of the last three decades. It is a rising tide of unauthorized appropriations. It is also worth noting that most of the current \$310 billion in unauthorized appropriations is funding programs whose authorizations has been expired for a decade or more. In fact, we continue to fund some programs whose authorization expired more than 30 years ago. That means we fund these initiatives whether they are accomplishing their goals or not.

## A Rising Tide of Unauthorized Appropriations



Appropriations have become increasingly divorced from authorizations, despite the presence of rule regimes in place in both chambers of Congress intended to prevent unauthorized appropriations. Senate Rule XVI and House Rule XXI create points of order against unauthorized appropriations. But these rules are not comprehensive, they are not self-enforcing, and they are rarely used in actual practice.

Consequently, the reauthorization of discretionary funded programs is itself becoming discretionary with the appropriations process increasingly blind to the authorization status of the various line items being funded. Instead of a bilateral system of authorization and appropriation with program funding contingent on both, we are moving toward a unilateral system. Again, I doubt it is coincidental that duplicative programs are proliferating along with the unauthorized appropriations. We are now funding 158 STEM education programs and nearly 700 renewable energy initiatives, according to the Government Accountability Office.

To be clear, I am not arguing that every program whose authorization is expired does not merit funding. But if appropriations are in no way contingent on authorization, we relinquish our responsibility to regularly review and reform programs. It is not enough for authorizing committees to act only to avert crises. That essentially sets discretionary spending on the same autopilot mode to which we have already set the two-thirds of the budget that consists of entitlements and other mandatory spending.

Ultimately, if we are going to cure our chronic overspending habit, we need to fix America's broken budget process, especially between the congressional authorization and the appropriation process.

I should mention that these expired expenditures are only where they listed a specific expenditure, not such sums or other things. We have programs that would run that total up considerably if all of those programs were thrown in. I hope we can find the solution today.

Senator Whitehouse.

#### **OPENING STATEMENT OF SENATOR WHITEHOUSE**

Senator WHITEHOUSE. Thank you very much, Mr. Chairman, and thank you, Director Hall, for appearing before us today. I was looking forward to hearing your testimony last month on CBO's revised budget outlook, but the blizzard superseded that hearing. So I will make the most of your participation today by focusing a little on CBO's projections in my opening remarks.

But, first, there is another matter that I would like to address. Director Hall is entitled to the benefit of the doubt, and he will have it. But a caution light blinks for many of us based on his background at the Mercatus Center, which the Washington Post described as a "staunchly anti-regulatory center funded largely by Koch Industries, Incorporated." In her recent book "Dark Money," journalist Jane Mayer wrote that Clayton Coppin, a professor at George Mason who reviewed Bill Koch's political activities, concluded Mercatus to be "a lobbying group disguised as a disinterested academic program."



This caution acquires particular force for some of us because of the novelty of dynamic scoring and the discretion that CBO has been given in this area. Dynamic scoring can be used selectively, for instance, to ease the passage of legislation like large corporate tax cuts, while ignoring growth or savings that come from investments on the spending side. CBO has a longstanding reputation for independence and provides a critical function to Congress. It is important that that not be compromised. I will say no more, and I am sure Director Hall understands.

I now want to turn to the budget outlook. As was widely reported last month, CBO projects the budget deficit will grow in 2016 for the first time since 2009. In describing a \$130 billion jump in its 2016 deficit calculation, CBO noted, "That increase is largely attributable to legislation enacted since August, in particular, the retroactive extension of a number of provisions that reduce corporate and individual income taxes."

While I supported the omnibus bill, I believe the tax provisions which cost over \$800 billion over 10 years, including interest costs, should have been paid for like any other spending increases. It is somewhat astonishing that Republicans insisted on offsetting the costs of \$80 billion in sequester relief but supported \$800 billion in tax spending with no offsets. Tax spending is real spending. As former Speaker John Boehner said, "We need to acknowledge that what Washington sometimes calls 'tax cuts' are really just poorly disguised spending programs that expand the role of Government in lives of individuals and employers."

Reagan economist Martin Feldstein agrees and noted, "Cutting tax expenditures is really the best way to reduce Government spending." I would add that tax spending is also a vector for big giveaways to special interests.

In the budget outlook, CBO projects revenue as a share of GDP will hover around 18 percent for the next decade. The last time we had budget surpluses at the end of the Clinton administration, revenue hit 20 percent of GDP. If we truly believe the deficit threatens future prosperity and are truly serious about wanting to tackle it, we are going to need to acknowledge that tax spending is part of the problem. Much of that tax spending is an Ali Baba's cave of treasure for special interests, and unlike one-time appropriations earmarks, special interest tax spending lives on and on and on in Ali Baba's cave. These, too, are permanent authorizations.

So far, Republicans have been unwilling to give up a single tax loophole in the cause of deficit reduction. Not a one. The super committee charged with replacing the harmful sequester cuts failed, in large part because Republicans refused to close any tax loopholes. Each time we have negotiated sequester relief, Democrats try to bring loopholes into the mix, and each time it is refused.

As the Senate-passed fiscal year 2016 budget resolution noted, tax expenditures for 2016 will total about \$1.5 trillion. By 2025, tax expenditures will rise to over \$2.2 trillion. We will spend more money on tax expenditures this year than we will spend on all Federal health care programs combined. We will spend, for instance, \$60 billion this year on the, shall we say, much discussed

Obamacare insurance exchange subsidies. But 25 times that amount will go out the back door of the Tax Code.

From the carried interest loophole for hedge fund managers to Tax Code subsidies for oil and gas giants, there is plenty of deficit reduction to be found in tax provisions designed to take care of wealthy and well-connected interests. Any sincere effort to cut the deficit must end egregious tax giveaways.

Turning to the topic of today's hearing, unauthorized spending is a symptom of broader dysfunction in the budget process. When you look at how difficult it can be to reauthorize even popular programs like the Violence Against Women Act, it is no surprise the Senate cannot keep up and that authorizations lapse.

Given institutional hurdles and partisan obstruction, we should consider whether it makes sense to have authorizations sunset or whether they should continue until repealed or replaced.

Finally, as we continue to examine process reforms, Budget Committee members need to have a frank discussion about the relevance of this Committee. In a Senate that requires 60 votes on any major legislation, the 60-vote penalty for violating this Committee's budget is meaningless, both to the Appropriations Committee and to the body. And I think the negligible attendance that we see at Budget Committee proceedings is not a signal of the fact that we are up on the sixth floor but a signal of the fact that everybody recognizes we really do not count for much any longer.

Mr. Chairman, I appreciate your leadership in exploring ways to improve the budget process and to revive the relevance of what should be an important Committee. As you contemplate a new budget resolution and budget process reforms, I encourage you to continue the spirit of open dialogue and of fostering bipartisan ideas, and I thank you.

Chairman ENZI. Thank you, Senator Whitehouse.

We know that the authorization process has been for many decades a key facilitator of programmatic oversight and reform. When we fund unauthorized programs, we keep the experts who sit on the committees of the authorization on the sidelines. We put too much of a burden on the shoulders of appropriators. We skip the budget. We become the sole arbiters of funding decisions, decisions often made under great duress after a fiscal year has already begun because the work did not get done timely. Congress should not abandon its fundamental responsibility to authorize and reauthorize what it funds. And I look forward to working with you on doing something about the budget process, too.

Our first witness today is Keith Hall, who is the Director of the Congressional Budget Office. Some of the data I cited in my opening statement comes from the most recent version of CBO's annual report called "Unauthorized Appropriations and Expiring Authorizations." CBO is required to issue this report each year under the terms of the Congressional Budget Act. Director Hall is the ninth CBO Director. He is an economist who formerly served as Commissioner of the Bureau of Labor Statistics, the Chief Economist of the White House Council of Economic Advisers and the Department of Commerce, and a senior international economist for the International Trade Commission.

Dr. Hall, thank you for joining us today to inform our discussion on these unauthorized appropriations. Dr. Hall.

**STATEMENT OF THE HONORABLE KEITH HALL, PH.D.,  
DIRECTOR, CONGRESSIONAL BUDGET OFFICE**

Mr. HALL. Chairman Enzi, Senator Whitehouse, and members of the Committee, thank you for the opportunity to testify about unauthorized appropriations. Since this is a technical subject, I will start with some background to make it clear to everyone what I will be talking about.

Legislative practices long differentiated the laws that establish Federal entities or programs from laws that fund them. Authorizing legislation is the first component of that practice, and appropriation laws are the second. Specifically, once the authorizations for the agency's programs or activities are in place, annual appropriation laws separately provide funding for them.

Authorizing legislation can take different forms. It can be organic or enabling legislation which broadly authorizes the creation and operation of an agency, program, or activity. Such legislation may or may not include an authorization of appropriations, which explicitly authorizes the funding for the agency program or activity.

Authorizations of appropriations can specify the amounts that may be appropriated for certain fiscal years or for an unspecified period. They can also indicate that the amounts are indefinite, authorizing the appropriation of such sums as may be necessary. If an authorization indicates either specific or indefinite amounts, I will refer to it as an "explicit authorization." Such authorizations are intended to offer guidance regarding the amount of funds necessary to carry out the authorized activities of an agency. Even when an explicit authorization of appropriations has expired, the organic legislation usually remains in place.

With that background, I will now discuss CBO's analysis of unauthorized appropriations. Each year, we provide the Congress with a report titled "Unauthorized Appropriations and Expiring Authorizations," as mandated by the Congressional Budget Impoundment Control Act of 1974. Last month, we published the most recent one known as the UAEA report covering fiscal year 2016. Our UAEA report seeks to identify programs whose explicit authorization of appropriations has expired.

For 2016, we reported that a total of \$310 billion, about one-quarter of discretionary appropriations in that year, was provided for programs and activities whose explicit authorization of appropriations had expired and whose appropriations could be identified. More than half of those unauthorized appropriations were provided for programs whose explicit authorization expired more than a decade ago.

I want to make four points about the UAEA reports.

First, the law requires CBO to prepare an annual report that identifies all programs and activities funded during a fiscal year for which authorizations of appropriations have not been enacted for that year. Our report includes only those programs whose explicit authorization of appropriations has expired. CBO cannot identify programs or activities that are receiving an appropriation even

though they have never had an explicit authorization of appropriations.

Our report sometimes identifies a program whose explicit authorization of appropriations has expired but not the amount appropriated because the program's funding is part of a larger appropriation account. Quite a few of those amounts are probably small, and some may be part of appropriations listed elsewhere in the report.

And, finally, even if the authorization of appropriations has expired, our report does not identify whether the organic or enabling statute governing a program or activity has expired. A permanent law may continue to set the policies and guidelines under which such appropriations are to be obligated. Identifying cases where enabling statutes never existed or have expired is not the focus of the law's requirement. To identify such cases among all programs and activities of the Federal Government would be virtually impossible.

To give a concrete sense of what is behind the numbers in our report, here are some examples.

When we issued our last report, the authorization of appropriations for several large agencies or programs had expired. This includes the National Institutes of Health, with appropriations of \$31 billion for 2016; NASA, with appropriations of \$19 billion for 2016. Even though the authorizations of appropriations for these programs have expired, organic legislation permanently authorizes the activities of those agencies. Those laws were most recently modified in 2007 for NIH, in 2010 for NASA.

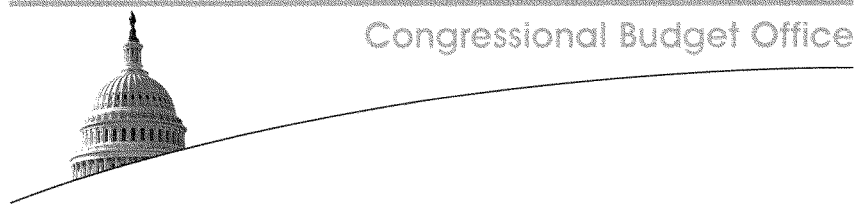
Some other large appropriations with expired authorizations of appropriations include the following: \$27 billion for programs authorized in the Violence Against Women and Department of Justice Reauthorization Act of 2005; \$26 billion for programs authorized in the Foreign Relations Authorization Act fiscal year 2003; and \$26 billion for programs authorized in the Quality Housing and Work Responsibility Act of 1998.

Expiration of authorizations for particular large agencies or large programs can significantly affect the changes from one year to the next in our report. For example, CBO reported that the total amount of unauthorized appropriations in 2008 was \$167 billion, but has been noticeably larger since then, averaging close to \$300 billion. That increase was attributable in part to the expiration of the 2009 authorizations of appropriations for both NIH and the programs in the Department of Justice that I just mentioned.

On average, over the past decade, about one-fourth of total discretionary appropriations were provided for programs and activities whose explicit authorizations of appropriations had expired.

I hope that you find this information helpful, and I am happy to answer any questions you have. Thank you again.

[The prepared statement of Mr. Hall follows:]



## **Testimony**

### **Appropriations With Expired Authorizations**

**Keith Hall  
Director**

**Before the  
Committee on the Budget  
United State Senate**

**February 3, 2016**

*This document is embargoed until it is delivered at 10:00 a.m. (EST) on Wednesday, February 3, 2016. The contents may not be published, transmitted, or otherwise communicated by any print, broadcast, or electronic media before that time.*

Chairman Enzi, Ranking Member Sanders, and Members of the Committee, thank you for the opportunity to testify on the subject of unauthorized appropriations. My statement today draws on the most recent of the Congressional Budget Office's annual reports titled *Unauthorized Appropriations and Expiring Authorizations*, known as the UAEA report, which was published in January 2016.<sup>1</sup>

### Summary

Spending authorizations are the first component of the long-standing two-part legislative practice of distinguishing between the laws that establish federal entities or programs that are to be funded through annual appropriations, and the laws that fund them. Once the authorizations are in place, funding for the agencies, programs, or activities is then provided separately in annual appropriation laws.

### What Are Unauthorized Appropriations?

The term "authorization" can mean organic or enabling legislation, which broadly authorizes the creation of an agency, program, or activity; "authorization" can also mean an authorization of appropriations, which explicitly authorizes the funding for an agency, program, or activity.

Authorizations of appropriations can specify the amounts that may be appropriated for certain fiscal years or indicate that the amounts are indefinite, authorizing the appropriation of "such sums as may be necessary." Such authorizations are intended to provide guidance regarding the amount of funds necessary to carry out the authorized activities of an agency. In most instances, even when an explicit authorization of appropriations has expired, the organic legislation remains in effect.

Broadly speaking, unauthorized appropriations occur when there is no current authorization for a program. CBO's UAEA report, which is mandated by the Congressional Budget and Impoundment Control Act of 1974, has a narrower focus: It seeks to identify programs that have had an explicit authorization of appropriations that has expired. The report does not list every program and activity that is funded without an authorization because tracking all expiring organic legislation would be virtually impossible; nor does the report include appropriations that may have an organic authorization but have never had an explicit authorization of appropriations. In

general, there is no well-defined categorization that links appropriations for many individual programs and activities to enabling authorizations.

### How Much Has Been Appropriated for Programs Whose Explicit Authorization of Appropriations Has Expired?

On average, over the past decade, about one-fourth of total discretionary appropriations were provided for programs and activities whose explicit authorizations of appropriations had expired. CBO's most recent UAEA report, which covers fiscal year 2016, reported that \$310 billion—about one-quarter of discretionary appropriations in 2016—was provided for programs and activities whose explicit authorization of appropriations had expired and whose appropriations could be identified. More than half of those unauthorized appropriations were provided for programs whose explicit authorization expired more than a decade ago.

The \$310 billion includes funding for many programs that have organic legislation in effect that broadly authorizes the program—for example, the activities of the National Aeronautics and Space Administration (NASA). That amount, however, does not encompass all of the programs whose explicit authorizations of appropriations had expired. Appropriations for some programs cannot be easily identified because they are part of a larger appropriation account. As a result, in its UAEA reports, CBO has been unable to identify the amount appropriated for many of the expired items; quite a few of those amounts are probably small, and some of them may be part of appropriations that are listed elsewhere in the report.

### Background on Authorizations

Authorizations define or reference the purposes for which appropriated money may be obligated and spent. The term "authorization" is used to describe two types of measures; both may—and often do—occur within the same law. One is an organic (or enabling) statute, which creates a federal agency, establishes a federal program, prescribes a federal function, or provides for a particular federal obligation or expenditure within a program. Such an authorization may provide an agency with the authority to obligate and spend federal funds in the form of direct—mandatory—spending.

The second type of authorization, which is the focus of CBO's UAEA report, authorizes the appropriation of funds. Such authorizations of appropriations can serve as a guide to the amount of funding necessary to carry out the authorized program or activity by including a specified dollar amount (called a definite authorization); or they may

1. Congressional Budget Office, *Unauthorized Appropriations and Expiring Authorizations* (January 2016), [www.cbo.gov/publication/51131](http://www.cbo.gov/publication/51131).

Table 1.

**Appropriations With Expired Authorizations, by Year**

	2007	2008 <sup>a</sup>	2009	2010	2011	2012	2013	2014	2015 <sup>b</sup>	2016
Unauthorized Appropriations (Billions of dollars)	n.a.	167	n.a.	291	n.a.	261	n.a.	302	294	310
Number of Laws	n.a.	214	n.a.	250	n.a.	259	n.a.	270	260	256

Source: Congressional Budget Office.

For 2007, 2009, 2011, and 2013, amounts could not be determined because temporary continuing appropriations covering most or all of the unauthorized programs were in effect when CBO issued its report.

n.a. = not available.

a. The National Defense Authorization Act for Fiscal Year 2008 was enacted on January 28, 2008, which was after CBO issued its report for that year. However, for purposes of comparison, the effects of the act have been excluded from the data in this column.

b. Full-year funding for programs within the Department of Homeland Security was not enacted when CBO issued its report for 2015. Therefore, totals for the department's unauthorized appropriations are omitted from this column.

authorize such sums as may be necessary to carry out the activity (called an indefinite authorization). Federal programs that have appropriations authorized in that way are generally known as discretionary programs because they require annual funding through the appropriation process.

Senate rules dating from the 19th century institutionalize the distinction between—and the proper sequencing of—authorization and appropriation bills. Whether an appropriation is unauthorized and whether it violates a Senate rule is determined by the Presiding Officer of the Senate on the basis of advice from the Office of the Parliamentarian. Although CBO's annual report is intended to aid the Congress by identifying those authorizations of appropriations that have already expired or will expire in the current year, the report is not and should not be considered definitive with respect to the application of Senate rules.

Until the mid-1950s, most authorizations were permanent and rarely included provisions that authorized appropriations for a specific dollar amount or period of time. In an effort to improve oversight and provide for periodic review of government programs, the Congress began to include temporary authorizations of appropriations in legislation that created new programs and to insert such provisions in the reauthorizations for many existing programs. That trend accelerated over the ensuing decades. However, the reauthorization of expired or expiring authorizations of appropriations sometimes was delayed—in some cases for extended periods, which resulted in a number of appropriations being unauthorized.

### CBO's Annual Report on Unauthorized Appropriations

By 1985, mounting concern over the perceived failure of the reauthorization process led the Congress to amend the Congressional Budget Act of 1974 to require CBO to report, by January 15 of each year, on the programs and activities that are funded each year without an authorization of appropriations.<sup>2</sup>

In preparing that report, CBO focuses on appropriations that are unauthorized because they have been provided for a program after that program's explicit authorization of appropriations has expired. However, as already mentioned, there is in most instances an underlying law—the organic, or enabling, statute—that governs the program and that typically is permanent. That permanent law continues to set the policies and guidelines under which appropriations are to be obligated, even if the authorization of appropriations has expired.

Under the definition of “unauthorized” used by CBO for its report, the total amount of unauthorized appropriations reported by CBO was \$167 billion in 2008. Since then, that amount has averaged close to \$300 billion (see Table 1). On average, over the past decade, about one-fourth of total discretionary appropriations was provided for programs and activities whose explicit authorizations had expired.

2. The report also identifies programs and activities for which an existing authorization of appropriations is due to expire, but that is not the focus of this testimony.

Table 2.

**Unauthorized Appropriations in Fiscal Year 2016, by the Last Year in Which the Program or Activity Was Authorized**

	1980- 2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Billions of Dollars	160	4	1	60	2	13	12	39	7	11

Source: Congressional Budget Office.

In the UAEA report for fiscal year 2016, CBO identified \$310 billion in appropriations that was provided for programs and activities whose authorizations of appropriations had expired and whose appropriations could be identified. More than half of those appropriations were provided for programs or activities whose authorization expired more than a decade ago (see Table 2).

The explicit authorization of appropriations for several large agencies or programs had expired when CBO issued its report, including the National Institutes of Health (NIH, with appropriations of \$31 billion for 2016) and NASA (with appropriations of \$19 billion for 2016). Both of those agencies have organic authorizations, however—NIH's in Title 42 and NASA's in Titles 42 and 51 of the U.S. Code.

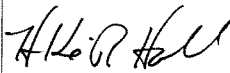
Some other large appropriations with expired authorizations of appropriations were those for programs authorized in the Violence Against Women and Department of Justice Reauthorization Act of 2005 (Public Law 109-162; \$27 billion), the Foreign Relations Authorization Act, Fiscal Year 2003 (P.L. 107-228; \$26 billion), and the Quality Housing and Work Responsibility Act of 1998 (P.L. 105-276; \$26 billion).

The 2016 report also lists many programs and activities for which a specific appropriation amount could not be identified. In those cases, activities were funded through larger appropriation accounts (for example, the health resources and services account of the Department of Health and Human Services), but the specific amount provided for the activity whose authorization of appropriations had expired could not be identified, either in the appropriations bill

itself or in supporting documentation. In those instances, the report noted that the specific dollar amount of the unauthorized 2016 appropriation was not available.<sup>3</sup> Many of those amounts probably are small and some of them may be part of appropriations that are listed elsewhere in the report.

3. In the process of preparing the annual UAEA report, CBO contacts authorizing committees, providing them with a preliminary list of the unauthorized appropriations under their jurisdiction. When CBO determines that no funds are being used for the program or activity or that it has been reauthorized, that program or activity is not listed in the report.

This testimony was prepared by Theresa Gullo and Janet Airis. The statement draws on the Congressional Budget Office's January 2016 report *Unauthorized Appropriations and Expiring Authorizations*. That report and the agency's other annual updates on the topic satisfy the requirements of section 202(e)(3) of the Congressional Budget and Impoundment Control Act, as amended. Jeanine Rees edited the testimony and prepared it for publication. It is available on CBO's website ([www.cbo.gov/publication/50955](http://www.cbo.gov/publication/50955)).



Keith Hall  
Director



Chairman ENZI. Thank you. I really appreciate the detail that you went into in this report. I think it will be very helpful. But one of the difficulties that we have around here is ever going back to look at anything we did in the past. We pointed that out with one hearing on old regulations, and these are old laws that we do not go back and revisit to see what changes need to be done. But I do appreciate the work that you and your staff did in this area. I think the findings are very illuminating.

I do want to highlight that the report only hints at the extent to which we are losing control over annual spending. As you pointed out, besides the \$310 billion, there are funds and activities that never received any explicit authorization.

Now, when Senator Coburn was here, I do not think he let any bills go through that did not have an explicit one in there so he would know how much was anticipated to be spent on that item. So a lot of them that are not expired that have specific sums in them are the result of the work that he did. He really did not like the words "such sums" or "funded at levels above authorized limits."

Is there a better way to measure the degree to which the annual appropriations are unchecked by the authorization process?

Mr. HALL. Well, we write that one of the problems is that we have not been able to look at programs that have no organic or enabling authority to exist at all, and getting a comprehensive list of those is very difficult. For example, trying to establish the linkages between appropriation accounts and authorizing statutes for everything would take really quite a long time. We certainly could work with you some to try to improve this report and maybe try to include more of that. I think something like a census is very difficult. If you sort of think about it, if we take every program that has an appropriation, in a sense we are trying to prove a negative. We are trying to establish that there is no authorizing language. So we have to go through all the laws to try to establish that nothing exists and then to do that for every appropriation.

So the perfect is probably impossible, but we certainly could do more to make this a better report.

Chairman ENZI. Well, another thing we discovered through the process is it was 260 expired authorization laws, but I think it was over 1,200 programs, because each authorization, again, to expedite being able to get through the whole process, I think we combine them a lot. And that also allows us to hide some of the things.

I am always looking for suggestions on how we can get Congress to go back and take a look at what we have done before. And we talk about such big numbers around here. I used to be a mayor, and on the city council, I know it took us longer to approve a shovel than it did street construction, and that is because everybody understood what a shovel was and how there are several different kinds of shovels, but they did not know much about street construction. So the street construction went right through, and the shovel took a long time. I suspect that is one of the problems with some of these things.

Now, your report inventories programs and activities that are explicitly authorized to receive annual appropriations for a duration of time. The time periods lapse, yet the funds continue to flow.

As a student of the political economy, do you find it troubling that the majority of the Government's nondefense discretionary spending funds programs and activities with lapsed authorizations? Should we just approve programs and let Appropriations decide all the priorities? Any suggestions?

Mr. HALL. Well, to say as a citizen, I think the country would be well served if Government activities of all kinds—discretionary spending, mandatory programs, and provisions of the Tax Code—were reviewed from time to time to make sure that they are being implemented effectively and to determine whether changes are necessary. I think going through a regular process of reauthorizing discretionary programs would certainly be one component of such a process, a useful component.

Chairman ENZI. Thank you. We are going to be looking at the process a lot more this year, as Senator Whitehouse suggested, and as we have held some other hearings. I will yield back the balance of my time. Since Senator Whitehouse is not here, I will go to Senator Perdue.

Senator PERDUE. Well, thank you, Mr. Chairman. And——

Chairman ENZI. Excuse me. Senator——

Senator WHITEHOUSE. No, no. Go ahead. Go ahead.

Senator PERDUE. No, please. Go ahead. I will yield to the Ranking Member.

Senator WHITEHOUSE. Well, that is kind of you.

I would like to go back to the point that I ended my remarks with about trying to sort of revive the relevance of the Committee and that as a larger issue around it, which is reviving the transparency of our spending.

When we are in crisis mode and our budgets are being worked out between the Speaker, the Majority Leader, and the President, then there is zero transparency in that. And I know from my perspective as a still somewhat junior Senator that trying to get the things you want to have a hearing in that conversation is virtually impossible. It is about as untransparent as you can, and things come in basically based on favoritism, clout, influence. I mean, it is kind of the worst of all possible worlds that we create for ourselves when there is not a proper process and there is just a crisis negotiation at the end.

Second best behind that is having the Appropriations Committees work through all their stuff and then have no proper floor work on what the appropriators propose to us, so that gets jammed down the rest of the body's throat, which is great for the appropriators but not so great for the body. And we have basically been gravitating back and forth between those two models virtually for as long as I have been here in the Senate.

And throughout all of that, the Budget Committee has been utterly sidelined because every appropriator knows that they are going to have to put a deal together that gets 60 votes. They cannot go forward until they have 60 votes. And once they know they have 60 votes, they know that there is nothing—it does not matter about our budget resolution. And then everybody else knows that as well. So when we do our budget resolution work, this room is empty but for the staff of the people who are condemned to be here and go through the exercise. And that is, I think, a pretty important signal

that nothing important is happening here when nobody shows up for it in a town that is immensely curious about the exercise of spending and power and so forth.

So I think that Chairman Enzi has done a really commendable service to this Committee by trying to open our aperture to focus on what our role is and how we can redefine ourselves. But whether it is entirely overlooking tax spending, having no transparent authorization—or very little transparent authorization process that is meaningful to the appropriators, and having appropriation run on cruise control even where there are no authorizations, it has really been a very dramatic collapse of the appropriating and funding function of this body into a very small group of people, and particularly at the crisis period, there is zero transparency.

I will close with where I started. As somebody who has to try to fight to get attention for programs into that process, and it is all—you know, you are calling people on the phone saying, “Can I get this in? Can I get this in?” And nobody knows what my motivations are, nobody knows what the other side of the argument is. I mean, the process completely stinks once it is in crisis mode. And so I hope that you, Mr. Hall, can help lead us along with the Chairman, and I think there is going to be a lot of support for it on our side, to have a conversation about how we can use this Committee to facilitate a broader and more transparent process for funding this enormous enterprise of the United States Government, both on the spending side and on the tax spending side.

Mr. HALL. Well, we are certainly happy to help in any way we can, and we are perfectly willing and we are—

Senator WHITEHOUSE. Do you concur generally with the points that I made about the lack of transparency and the lack of effective—the lack of transparency on the spending side and the lack of impact or import to our budgeting effort?

Mr. HALL. Well, we constantly have some issues in our work where we are trying to be helpful and offer advice to committees in a confidential way. But then when things become public, a bill or a proposal becomes public, we have a very important transparency practice where we try to create a level playing field and make our estimates public.

Senator WHITEHOUSE. Yes.

Mr. HALL. And we send it to both sides, and hopefully that—

Senator WHITEHOUSE. I think at this point your most valuable function, given the general lack of impact that this Committee has or import of this Committee, is that information-providing function. And I think the transparency of that information and the reliability of CBO information has a very healthy effect throughout our process. But once you get past information into actually doing something, that is where I think it is down to either the four guys in the room during the crisis or the appropriators and particularly the cardinals in their appropriations process for an omnibus.

Mr. HALL. Well, we certainly keep trying to do our best to create transparency in what we do and help further, if you like.

Senator WHITEHOUSE. Yes, I appreciate that.

Chairman ENZI. Senator Grassley was here at the sound of the gavel, so we will go to him, and then Senator Perdue and then Senator Ayotte.

Senator GRASSLEY. First, before I ask questions, let me confess, as Chairman of the Judiciary Committee, I see on a list of committees that we are fifth or sixth with about \$30 billion of that figure of unauthorized. And as Senator Whitehouse and I have worked so hard on reauthorizing the Juvenile Justice Reform Act and getting that done in our Committee about 6 months ago and still do not have it through the Senate, it just seems like it is going to take a long time to get work done that ought to be done.

But with that caveat, it seems to me that appropriators are really the only committees spending time reevaluating lots of these programs. So my question to you: Do appropriators evaluate programs at a level equivalent to what an authorizing committee should do if the authorizing committee did its job?

Mr. HALL. Well, for me personally, I do not have enough experience to answer that. One of the things that we hope is that our report is a good starting point. It is imperfect, but it is a good starting point if you want to start looking at this issue of sort of matching authorizations and appropriations.

Senator GRASSLEY. Another question: Is there an argument here for biannual budgeting so that more time can be spent on oversight and reauthorization efforts?

Mr. HALL. Well, I hesitate to offer advice on something like that. We certainly would be happy to accommodate whatever type of budgeting that you decide.

Senator GRASSLEY. Let me go to a rhetorical question, if I am asking you questions that you cannot give advice on. Our country is \$19 trillion in debt. The 2016 deficit has been projected to increase that by \$544 billion. What message are we sending to the American people that with this dire financial situation we cannot find the time to evaluate and scrutinize existing programs? If Congress does not do the necessary oversight that reauthorization requires, how can anyone trust that valuable fiscal resources are being used for the highest priorities? You surely can speak to that point.

Mr. HALL. Well, sure, and this is where we hope our annual budget forecast is useful, because the exercise of looking at what the budget is going to look like, say, over the next 10 years under current law and what sort of deficits that we are going to have I think is a useful thing. It is a useful thing to remind people that this is an issue. And something that CBO has said for a long time is that this is on a trend that is not sustainable. At some point the debt is going to get to a level where there are going to be real problems. It may not happen soon, but it is going to happen at some point unless there is some change.

Senator GRASSLEY. Since you have studied this issue that comes up with the \$310 billion figure of programs unauthorized, and you have to look at the entire Federal budget programs of \$3.6 trillion, I guess, would you categorize the \$310 billion as essentially low-hanging fruit that we ought to be able to deal with? Or do you think it is more complicated than that?

Mr. HALL. Well, it is low-hanging fruit in the sense that we know about it. You know, one of the real difficulties here is this idea of trying to match the authorizations and the appropriations because there is just so much law and there are so many things in the Fed-

eral budget. But these are things that hopefully this is useful to give you some idea of where there are issues and you can deal with these. We may not be able to give you a real feel for the overall size of the problem because this is not a comprehensive report. But it does give you a starting point, I think.

Senator GRASSLEY. Mr. Chairman, thank you, and I will yield back my time.

Chairman ENZI. Thank you.

Senator Perdue.

Senator PERDUE. Well, Mr. Chairman, thank you for holding this hearing, and, Dr. Hall, thank you for being here again. You know that—I said this the last time you were here—I am a big fan of your work. Thank you for all you are doing to enlighten us about our crisis.

But I disagree on one thing, and I will come back to my point, and then I have a couple questions. I do not think this is going to hit us soon. I think it is here right now. And the bellwether of that is what happened in December. Just a quarter point increase in our Fed fund rate will indirectly lead to a potentially increase in our Federal interest of almost \$50 billion. So the question I have is, you know, what happens if interest rates go back to our 50-year average of just 5 percent? We have all seen interest rates much higher than that, but we have lived in an arbitrarily flat interest world in the last 7 years. It is just not forecastable. We cannot assume that going forward.

So we know that interest rates are going up. We know that our interest expense is going up. And yet we sit in an environment where last year we saw our Federal expenditures at \$3.7 trillion, up from—just in 2000 in constant dollars it was \$2.4 trillion. And you might say, well, we are spending more on military. Only \$100 billion of that increase was military. The rest of it is growth in mandatory expense.

So we have got a situation today where it almost feels to me like—and God help me, I have been here a long time. I finally found something that Senator Whitehouse and I agree on, and I absolutely agree that the process is broken. The 1974 act has only worked four times in 40 years. It has not worked. It is not working. It will never work. And I feel like sometimes we are sitting around here talking about the layout of the chairs on the Titanic. There is no question we have got redundant agencies, no question we have agencies that have not been authorized. But the system of budgeting, authorization, and appropriation by definition was never going to work. It is not working, and so we have got to change that fundamental process.

Having said that, we saw a report from the Comptroller General of the GAO recently talking about redundant agencies. Have you worked and can you work with the GAO to help us better understand the priorities and maybe the overlap between those unauthorized agencies and the redundant agencies that have been identified?

Mr. HALL. Sure, we are happy to contribute however we can.

Senator PERDUE. Okay, because I think, you know, the question is: How big of a Federal Government do we need? If we have redundant agencies, there is an opportunity. We talk about tax ex-

penditures, but we raised \$3.2 trillion last year in Federal revenue. That is the largest ever. And I do not disagree that there are issues around deductions and so forth where we have corporate welfare issues and that sort of thing that are affecting our ability to deal with this. But, honestly, until we get at this authorization process leading into an appropriation process that, frankly, is not working—it did not work last year; it led into an omnibus, just like it has in prior years—that increases our spending. Your own report shows that we are adding some \$8.5 trillion to the debt over the next decade, if I read the report correctly.

What should we be doing in terms of prioritizing our approach? You do the measurement for us, but you also can model and look at things. Where is the low-hanging fruit in terms of going after this absolute crisis that we have today?

Mr. HALL. Well, one of the things we do certainly in the outlook is we want to give you some idea of what the problem is, you know, sort of what trend we are on. It is certainly sort of not our role to sort of recommend things, but we did produce—and we did produce near the end of last year a number of budget options to give you some idea of the different things that you can do to improve the deficit situation, some idea of what sort of impact it would have. So it is sort of a listing of things you can look at, tools that you have at your disposal. I think that is really worth looking at and getting a feel for what sort of options you have going forward.

Senator PERDUE. Well, do you work with GAO at all to model some of their recommendations and ideas?

Mr. HALL. We do interact with GAO a bit. I do not know that we interact a lot on things.

Senator PERDUE. Well, Mr. Chairman, I just—I mean, I absolutely applaud what you are doing here in terms of looking at this authorization issue. And I know that we are moving down a road that is really a bipartisan effort. I agree with Senator Whitehouse. I mean, this is not about partisan politics. This is about a crisis that is threatening our very ability to defend our Nation. And it puts in jeopardy the very safety net programs that we all want. Social Security and Medicare, as we all know, absolutely their trust funds go to zero in 15 years. And yet we have not—I have been here a year. We have not had any salient conversations about how to save Social Security and Medicare. And those are the two things, as I look at your report, that are just exploding away from us in the next 10 years. And if you go out 10 more years, it really gets to the point of being unmanageable. I contend that it is already unmanageable, and I look forward to further hearings like this and to actually move toward getting results.

I will just end with this. There are four words that I have not heard up here in one year that I used to hear every day in business, and that is, “We cannot afford it.” We all do it in our personal homes. We do it in our personal lives. We teach our children to do it. And yet we run a Federal Government where we absolutely do not consider that.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

In our method of alternating, Senator Kaine will be next, then Senator Ayotte.

Senator KAINE. Mr. Chairman, I would defer to Senator Ayotte to be next since I just walked in and am collecting my thoughts, unless she wants me to go first.

Senator AYOTTE. Thank you so much. I really appreciate it.

Senator KAINE. Okay.

Senator AYOTTE. Thank you, Senator Kaine.

Chairman ENZI. Very nice of you. Thank you.

Senator AYOTTE. Thank you, Chairman.

You know, I am going to suggest something that is a heresy around here, actually, and I have suggested it before. But I serve on the Armed Services Committee, and every year we do a defense authorization. It is very bipartisan. We spend a tremendous amount of time going through each of the programs, each of the weapons systems, the pay and compensation for our troops, and we have consistently voted a bipartisan bill out and then got it to the Senate floor every year.

But here is what happens. Then the Appropriations Committee takes it up, and they spend lots of money on things that were never authorized, were never supported, and we spent a ton of time working on it. So I have suggested this before—this always gets me in trouble, but I do not see how the dual system of authorizing and appropriating actually benefits effectively spending Federal dollars, because if the authorizing committees had to take responsibility for actually how the money went out the door, and they are specializing in these areas, I actually think there would be much more regular routine authorizations, there would be more oversight, because the two are totally disconnected. It is unbelievable. We do a whole hearing on a program that is absolutely—I remember this. I was new in here. It was called—I dubbed it “the missile to nowhere.”

No results, no money, we were pouring billions of dollars in something that we are not going to get a result on, and then it just gets slipped back in. We were unanimous in the defense committee after having, you know, lots of work done on it, and then it just gets slipped back in.

So I guess you—one of the things that you identified in this report, as you were just testifying, it was hard for you to match the appropriations with the authorizations because we have this dual process. So I know that you probably cannot render an opinion on this, but I just want to say that as we look at fundamental reform around here, I know this is a very controversial thing to say, but this dual process is not doing a service to the American people in terms of oversight. Would you agree with me, though, you did have difficulty matching up the appropriations and the authorizations because the two almost—one is from Venus and one is from Mars?

Mr. HALL. Well, yeah, that is right. And to some degree, we are picking the low-hanging fruit, to be honest.

What we did not include is actually much harder to get a hold of.

Senator AYOTTE. Right. So now that I have gotten myself in a lot of trouble here, I want to also talk about the GAO piece—because I think this is really very important—that Senator Perdue talked about because this is something that I have been focusing on. I have a bill with Senator Manchin called the “Duplication Eliminate

Act,” which would actually force the executive branch and the Congress to take up what the GAO is doing. Basically, the GAO since 2011 has issued an annual report on ways to reduce duplication, overlap, fragmentation in Federal Government. In their first five reports, GAO has identified about 500 opportunities to reduce duplication, overlap, and fragmentation, but yet only 29 percent of GAO’s recommendations have even been touched upon or addressed in any way. And they add up to a lot of money. Just as an example, addressing just one of GAO’s recommendations on Medicare payment policy would have saved an estimated \$3.2 billion to \$5.1 billion from 2010 to 2012.

So to Senator Perdue’s question, how do we get to this issue of actually taking up the work that you have done in CBO, aligning it with the work that GAO has done, and really actually getting to the work of implementing the GAO policies and having greater oversight and hopefully greater authorization work?

Mr. HALL. Well, certainly we have a role in sort of evaluating proposals on how to do some things like this, and we are happy to help, and we are happy to do our usual sort of evaluation of things like that. We do not work too directly in GAO on this particular issue, but we certainly can help in the solution.

Senator AYOTTE. Well, I think it would be helpful if there was some alignment there, just because they have done a lot of good work. We need to get off our butts and take up more of their work, but also if CBO could also incorporate that work of ways we could save money and working together, I think it would be helpful to really getting us to focus on this more. And I hope that we do, because as we look at a lot of programs that not only have not been authorized, they have not been evaluated in years. There have not been any metrics or measures. There are lots of agencies doing the same thing. And it seems to me that this is an issue that is very bipartisan that we should be more effectively addressing.

Thank you.

Chairman ENZI. Very good. Thank you.

Senator WHITEHOUSE. Chairman, may I seek recognition at the conclusion of Senator Kaine’s questioning of the witness in order to respond to Senator Ayotte’s thoughts?

Chairman ENZI. Sure.

Senator WHITEHOUSE. Thank you.

Chairman ENZI. Senator Kaine.

Senator KAINE. Thank you, Mr. Chairman, and thank you, Director Hall. It is good to have you with us.

The change in the CBO’s outlook from August to January have been significant based on your recent report. Some of this change is driven by economic trends, but a dramatic amount of the change, especially as it relates to the deficit, was driven by legislative changes at year-end. And if you look at this kind of on a percentage basis and affecting the deficit by our calculation, the bill that we passed in December was the fifth largest deficit-increasing bill since 1986.

The amount of debate that we had about that bill was interesting. There were minimal spending increases which were largely, though not completely, paid for. But there was a tax extender package of tax expenditures that was not paid for at all. And so the pat-



tern that I think is interesting—the title of this hearing is “Spending on Unauthorized Programs”—is that we have developed sort of an internal rule that we have got to pay for spending, but we do not have to pay for tax cuts. And I think that is problematic.

I agree with the goal that we should be analyzing and reviewing and reauthorizing spending. I agree with that. Before the 1950s, the norm was not to reauthorize spending, put spending in the budget and it just stayed there. There were not the sunsets and the reauthorization periods. But after the 1950s, we moved into at least the notion of reauthorization. Whether we did it or not, at least that was set up as a norm. But I do not think in the Tax Code we have yet developed an expectation that tax cuts, tax policies be reauthorized as well.

Eighty percent of the deficit effect of the act we passed at year-end 2015 was on the tax expenditure side, not on the spending side. Eighty percent of the deficit effect. So I want to ask you, Director Hall, would it be fair—is there sort of good for the goose, good for the gander? If we are going to be in the reauthorizing business and the reanalysis business, shouldn't we treat a tax expenditure in the same way we treat a program expenditure and have a normal practice of reanalyzing and reauthorizing all of them?

Mr. HALL. Well, we try to stay out of offering advice on things like that.

Senator KAINE. You cannot blame me for trying, though.

Mr. HALL. Right. But I appreciate the notion, and, you know, we do have a little information on the tax expenditure, information from the Joint Committee on Taxation in our report to give you some idea of how that changes from year to year.

Senator KAINE. But, you know, is there any reason why from your standpoint, kind of a budget office standpoint, should we treat tax expenditures completely differently than program expenditures? Or shouldn't, you know, we be in the business, if we are going to be reanalyzing and reauthorizing, of looking at all of it?

Mr. HALL. Well, again, I hesitate to offer advice.

Senator KAINE. How about separate from the advice, is there an economic difference or a budgetary difference between a program expenditure and a tax expenditure that would warrant the need to, you know, continually reauthorize and reexamine program expenditure but not do that on the tax expenditure side?

Mr. HALL. Well, certainly one of the points that we make and we have made for a long time on the outlook and all our budget forecasting is that, given the current trend towards increasing deficits, we need to either raise revenues, lower spending, or both. And something pretty significant needs to be done to stop the trend that we are on, and it needs to be something that is not small. It needs to be things that are large.

Senator KAINE. I am going to associate myself with the “or both” category. I do not think you can deal with a balance sheet if you just put, you know, a blindfold on one eye and say, “I am just going to look at one-half of the balance sheet.” You just cannot do it. You cannot look at either half of the balance sheet in exclusion and deal with the challenges that we have. But I think we have kind of gotten into a pattern where we are just looking at one-half of the bal-

ance sheet. And so, you know, looking at the CBO's report about the deficit effect of the December action and digging into it further and finding that 80 percent of the deficit was driven by the tax expenditure side, not by the program spending side, I found that pretty sobering. And I think in terms of, you know, the kind of reform—I hope the Budget Committee can use this year where we did a 2-year budget to really be about some reforms, and I think a reform in this area would be very, very valuable.

With that, thank you, Director Hall, and thank you, Mr. Chair. Chairman ENZI. Senator Whitehouse.

Senator WHITEHOUSE. Thank you, Chairman. I thought that Senator Ayotte's point was a particularly good one, and as I was thinking about it, it struck me, to my earlier point, that a budget point of order against an appropriations bill that blows through the budget that this Committee has gotten passed is a useless effort because it gets overcome by a 60-vote vote. And if the appropriators have lined up 60 votes, which they have now because everything has to pass by 60, then there is a null effect of the point of order that the budget has been broken.

I suspect that the same is true of a point of order that they are appropriating authorized funds, and so I think there are colleagues of ours, particularly those who serve on the Appropriations Committee, who would object pretty violently to the proposal that the Appropriations Committee is no longer useful and we should have appropriations done at the authorizing level. Even if that were the right thing to do, it would be hard to convince some of our colleagues of it.

But I do think that if we were to think about how we reimposed a penalty beyond the 60-vote margin—because the other thing that has happened in all of this is that the person who gets the 67-vote penalty is the President of the United States, because we would have to come up with 67 votes to overcome a veto.

So when we cannot control it amongst ourselves because the appropriators control 60 votes and budgets authorizing, nobody else matters, the one person who then matters is the President. And that creates an enormous transfer of power from Congress to the Presidency. So particularly for those who decry the power of this particular President, we have actually really loaded him up with huge amounts of power by having the one—he being the one place where we have to get to 67, the one person who can be a check on appropriators.

So it is a conversation I think we need to continue to have in this Committee, but I do think this question of there being, in effect, no penalty for violating authorizations and no penalty for violating budgets is a problem. And it is part of this process that has taken our spending and put it into a very dark hole. And the longer we wait and the bigger a crisis, the smaller number of people in the hole and the darker it is, and the more who knows what gets stuffed into the deal.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you, and this is the prime time to be talking about this. Right now what we are doing is defining that there is a problem, and we will get into some solutions, and the solutions could take effect at the beginning of next year, because

none of us know what next year is going to be like. And so I think it will lead to us all being reasonable. That is my hope.

On the programs, it is possible to do something about them. When I was Chairman of the Health, Education, Labor, and Pensions Committee, I discovered that we had 119 preschool programs—they were all named after some Senator—and there was a lot of duplication. So Senator Kennedy and I were able to get that down to 69. Since that time, we have been able to get it down to 45. And there are always proposals for additional preschool programs because there is evidence that they do good work.

Senator WHITEHOUSE. Does it help, Mr. Chairman, when the Senator who it is named after retires?

Chairman ENZI. They still come to see you. [Laughter.]

What helps is if you can get them to go take a look at what has happened with their program and find out that instead of an education program, it is a babysitting program. That is an important program, too, but it is a different expense. So we need to do some things.

Thank you, Dr. Hall, for your help today and particularly for your great document, which I hope we can make good use of to make some great changes for Government.

So while we are setting up the next panel, I will introduce the witnesses that will be appearing.

We have Jessica Tollestrup, who joins us from the Congressional Research Service, CRS, which is the research arm of this Congress. Ms. Tollestrup is an analyst on Congress and the Legislative Process for CRS. She has authored several recent papers concerning the history of the authorization and the appropriations processes and the internal rules the Congress has created to police its own funding of unauthorized appropriations.

Paul Posner is a professor of public policy at the George Mason University, where he founded and directs the Center on Public Service. Dr. Posner is a recognized Federal budget policy expert. He formerly served as the Director for Budget Issues in the Accounting and Information Management Division of the Government Accountability Office.

And James Thurber is the University Distinguished Professor of Government and founder and director of the Center for Congressional and Presidential Studies at American University here in Washington, D.C. I should note that Dr. Thurber has served in this body at the staff level, including as a legislative assistant for the late Senator Hubert Humphrey.

So if we can have you take your places at the table there, and we will begin with Ms. Tollestrup. Did I get the name right?

Ms. TOLLESTRUP. Yes.

Chairman ENZI. Thank you.

**STATEMENT OF JESSICA TOLLESTRUP, SPECIALIST ON CONGRESS AND THE LEGISLATIVE PROCESS, CONGRESSIONAL RESEARCH SERVICE**

Ms. TOLLESTRUP. Mr. Chairman, Ranking Member, and members of the Committee, my name is Jessica Tollestrup, and I am a CRS Specialist on Congress and the Legislative Process. Thank you for inviting me to speak with you.

I would like to start by briefly stating four main points from my written testimony that I will expand on in my remarks today.

First, authorizations of appropriations are a tool that the authorizing committees have developed in recent decades to engage in legislative oversight and better influence appropriations decision-making.

Second, those authorizations of appropriations may lapse for a number of reasons that are not directly related to whether that purpose should continue to receive funding.

Third, the prohibition on unauthorized appropriations in Senate rules applies only to floor amendments. It does not apply to reported appropriations bills or committee amendments.

Fourth, addressing expired authorizations through consequences that are felt in the appropriations process has inherent challenges, but so, too, does approaching this issue as part of the authorization process.

I also want to start by clarifying that there are two types of authorizations:

First, there are authorizations that establish the authority for Federal Government activities. Those authorizations provide a sufficient basis for Congress to later fund those activities.

Second, such authorizations are also occasionally accompanied by another type of provision, an explicit authorization of appropriations. If this second type of provision lapses, the legal requirement that the Federal Government undertake the activity is generally still in effect. However, appropriations for those activities would usually be regarded under congressional rules—but not for legal or constitutional purposes—as being unauthorized.

Now for my first point. The purpose and form of authorizations has changed in a number of important ways over the past 100 years. During the 19th and early 20th centuries, authorizing laws generally provided broad grants of authority on a permanent basis and usually did not include specific amounts to be appropriated. After the 1920s, the authorizing committees began to alter these practices and increasingly included two components in authorizing laws: the authority for the activity and also language that essentially recommended a funding level for that activity through an explicit authorization of appropriations.

Later, those committees began to conduct reviews and periodically enact revisions to certain authorizations. While the timing of these revisions often coincided with the need to reauthorize appropriations, these revisions also provided an occasion to conduct legislative oversight and make needed programmatic changes.

While the proportion of agencies and programs that were subject to periodic reauthorization expanded significantly during the mid-20th century, variation has continued an approach in practice. Many agencies and programs are still authorized on a permanent basis, and others have experienced different reauthorization schedules at different times. Also, in an increasing number of instances, periodic authorizations of appropriations have lapsed or not been renewed in a timely manner. This occurs for a variety of potential reasons.

For example, a lapsed authorization of appropriations could indicate that the authorizing committee has decided that no pro-

grammatic changes are needed at this time. Another possibility is that Congress has not yet achieved consensus as to what changes should be made. This presents a challenge when Congress attempts to assess the meaning of expired authorizations of appropriations, especially when the primary procedural avenue to address them is part of the appropriations process.

Although both House and Senate rules prohibit unauthorized appropriations, these rules are primarily enforced for floor amendments. While this procedural mechanism has the potential to encourage the timely enactment of reauthorizations, one challenge is that addressing expired authorizations themselves is not within the control of the Appropriations Committees.

In addition, this framework can effectively set up a choice between delayed appropriations and funding unauthorized programs. As a result, this mechanism's effectiveness is limited when appropriations are unauthorized for reasons that are not directly related to whether that purpose should be funded.

Attempting to address this issue through the authorization process is also challenging. There are no congressional rules that govern the form of authorizations, and the responsibility for authorizations is divided among a number of committees.

In addition, a committee may choose its approach to an authorization based on a number of factors, including its assessment of the current needs of the program, historical practices, and the legislative environment.

On the one hand, this lack of chamber rules gives committees the flexibility to structure each authorization to meet their particular needs. On the other hand, this flexibility makes addressing expired authorizations on a widespread basis more difficult.

Thank you, and I would ask that the full text of my prepared statement be submitted for the record.

[The prepared statement of Ms. Tollestrup follows:]



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**TESTIMONY**

Statement of

**Jessica Tollestrup**

Specialist on Congress and the Legislative Process

Before

Committee on the Budget  
U.S. Senate

Hearing on

## **“Spending on Unauthorized Programs”**

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Mr. Chairman and members of the committee, thank you for your invitation to appear today to offer testimony with regard to the historical development of some of the congressional rules and practices related to authorizations and appropriations. Specifically, this testimony addresses the relationship between authorizations and appropriations in the congressional budget process and how the purpose and frequency of authorizations has evolved over the past two centuries. It concludes with a discussion of how the House and Senate approach appropriations not authorized by law in their rules and associated practices.<sup>1</sup>

## The Relationship Between Authorizations and Appropriations

### Authorizations and Appropriations Distinguished

The U.S. Constitution grants Congress the “power of the purse” by prohibiting expenditures “but in Consequence of Appropriations made by Law.”<sup>2</sup> As a result, legislation to provide for government expenditures must adhere to the same requirements and conditions imposed on the lawmaking process as any other measure. The Constitution does not, however, prescribe specific practices or procedures. Instead, the manner in which the House and Senate have chosen to exercise this authority is a construct of congressional rules and practices, which have evolved pursuant to the constitutional authority of each chamber to “determine the Rules of its Proceedings.”<sup>3</sup> One way in which both chambers have chosen to exercise this authority is to adopt rules that limit appropriations to purposes authorized by law. This requirement allows Congress to distinguish between legislation that addresses questions of policy and legislation that addresses questions of funding—and to provide for their separate consideration. In common usage, the terms used to describe these types of measures are “authorizations” and “appropriations,” respectively:

- An *authorization* may generally be described as a statutory provision that defines the authority of the government to act. It can establish or continue a federal agency, program, policy, project, or activity. Further, it may establish policies and restrictions and deal with organizational and administrative matters. It may also, explicitly or implicitly, authorize subsequent congressional action to provide appropriations. By itself, however, an authorization does not provide funding for government activities.
- An *appropriation* may generally be described as a statutory provision that permits a federal agency to incur obligations and make payments from the Treasury for specified purposes, usually during a specified period of time.

From the beginning, Congress has observed the practice of considering appropriations separately from other legislation. As this practice developed, the distinction between appropriations and other types of legislation was reflected in the designation of measures containing budget authority for more than one purpose as “supply bills,” highlighting their purpose as supplying funds to carry out government operations already established in law. The House established formal rules in 1837 that stated, “No appropriation shall be reported in such general appropriation bills, or be in order as an amendment thereto, for any expenditure not previously authorized by law.”<sup>4</sup> These rules were motivated, at least in

<sup>1</sup> This testimony is largely drawn from CRS Report R43862, *Changes in the Purposes and Frequency of Authorizations of Appropriations*, by Jessica Tollestrup; and CRS Report R42098, *Authorization of Appropriations: Procedural and Legal Issues*, by Jessica Tollestrup and Brian T. Yeh.

<sup>2</sup> Article I, §9.

<sup>3</sup> Article I, §5.

<sup>4</sup> Asher C. Hinds, *Hinds' Precedents of the House of Representatives of the United States* (Washington: GPO, 1907-1908), vol. 4, §3578.

part, by concern over the increasing delays in enacting appropriations due to the inclusion of “debatable matters of another character.”<sup>5</sup> The Senate did not formally adopt a parallel rule until 1850, when it prohibited certain amendments to general appropriations bills that would propose additional appropriations unless it was for the purpose of carrying out the provisions of existing law.<sup>6</sup>

While the form and specific applications of these rules have evolved over time, their basic principles still persist in the rules of both the House and Senate today.<sup>7</sup> One effect of these rules has been the formalization of funding decisions as a two-step process in which separate legislation to establish or continue federal agencies, programs, policies, projects, or activities is presumed to be enacted first and is subsequently followed by legislation that provides funding. Another effect of these rules has been a distinction between appropriations authorized by law and those not authorized by law.

### “Authorized” and “Unauthorized” Appropriations

Under the rules of the House and Senate, whether an appropriation is “authorized” or “unauthorized” is determined based on the application of the precedents of the respective chamber; the existence of legislation defining the legal authority for particular federal agencies, programs, policies, projects, or activities; and the relationship of such authority to the applicable appropriation. In most cases, an appropriation is said to be authorized when it follows explicit language defining the legal authority for a federal agency, program, policy, project, or activity that will be applicable in the same fiscal year for which the appropriation is to be enacted. In contrast, an appropriation is said to be unauthorized when no such authority has been enacted or if authority that was previously enacted has terminated or expired.

When applying these House and Senate Rules in a particular context, additional distinctions related to the structure and specificity of the particular authorization in question is often relevant. House and Senate rules do not prescribe the form in which programs or activities are authorized, and, as a consequence, this structure and specificity varies widely in practice. The issue of structure includes whether the statute authorizing the program also explicitly authorizes appropriations for the program or does so implicitly. It is generally understood that statutory authority to administer a program or engage in an activity—sometimes referred to as organic or enabling legislation—also provides implicit authorization to appropriate for such program or activity even in the absence of an explicit authorization of appropriations. If an explicit authorization of appropriations is present, however, it may expire even though the underlying authority to administer such a program or engage in such an activity does not. If that authorization of appropriations is not renewed, subsequent appropriations are often regarded as unauthorized.

The interaction between authorizations and appropriations can also be affected by how specific or general an authorization is. For example, some statutes that provide an explicit authorization of appropriations place a limit on the amount that is authorized, either generally for a class of programs or activities or for a more specifically designated program or activity. In these instances, appropriations in excess of such limits are generally considered to be unauthorized. However, appropriations that address only some of the activities framed more generally in the authorization of appropriations, or do so in more specific terms,

<sup>5</sup> Ibid.; *Congressional Globe*, 24<sup>th</sup> Cong. 1<sup>st</sup> sess., p. 20.

<sup>6</sup> As the House has historically claimed the exclusive right to originate appropriations bills, the Senate expects to consider appropriations in the form of amendments to House bills. See William Holmes Brown, Charles W. Johnson, and John V. Sullivan, *House Practice: A Guide to the Rules, Precedents and Procedures of the House*, 112<sup>th</sup> Cong., 1<sup>st</sup> sess., (Washington: GPO, 2011), ch. 4, §2.

<sup>7</sup> These prohibitions are currently located in House Rule XXI(2)(a) and Senate Rule XVI(1). For further information on the operation of these rules, see CRS Report R42098, *Authorization of Appropriations: Procedural and Legal Issues*, by Jessica Tollestrup and Brian T. Yeh, pp. 4-8.



are said to be authorized so long as the appropriation falls within any limits prescribed by the authorization.

## The Evolution of Purposes and Frequency of Authorizations

The choice to separate money and policy decisions and vest control over them with different congressional committees has meant longstanding tensions between the authorization and appropriations processes. These tensions have significantly influenced how the processes have evolved as Congress has exercised its lawmaking and oversight prerogatives to affect decisions related to federal government activities and the level at which those activities should be funded.<sup>8</sup>

### Development in the 19<sup>th</sup> and Early 20<sup>th</sup> Centuries

From the very earliest Congresses, authorizations were generally used to provide permanent, broad grants of authority, while control over the details and amounts for particular activities was achieved through the annual appropriations process. During this period, authorization for subsequent congressional action to provide appropriations was implicit and did not include specific amounts to be appropriated. Temporary authorizations were rare and were generally reserved for programs that were intended to be of a limited duration. In contrast, appropriations laws contained the details of what agencies were able to do and how much they would have to spend.<sup>9</sup> These appropriations laws were enacted annually.

Developments in the House and Senate committee systems that occurred during this same period also served to strengthen this authorization-appropriations distinction. At first, the “legislative committees” had jurisdiction over authorization measures, while the House Ways and Means Committee and Senate Finance Committee were responsible for most appropriations bills. During the Civil War, however, when the workload of these committees and size of federal expenditures increased considerably, both chambers chose to create separate Appropriations Committees that would be responsible for the annual appropriations measures.<sup>10</sup> Although jurisdiction over some appropriations was dispersed during the late 19<sup>th</sup> century, Congress continued to keep appropriations measures separate and distinct from authorizations.<sup>11</sup> The reconsolidation of appropriations jurisdiction and the reorganization of regular annual appropriations bills in the House in 1920 (and in the Senate in 1922) further reinforced this distinction.<sup>12</sup>

As the size and scope of federal government activities increased, the congressional practices related to authorizations and appropriations began to change. Authorization laws began to specify the details of broad classes of federal government programs and activities in consolidated legislation instead of in multiple pieces of stand-alone legislation that addressed only some aspects of such programs and

<sup>8</sup> The summary that follows of the general development of these congressional rules and practices is largely based on Alan Schick, *Legislation, Appropriations, and Budgets: The Development of Spending Decision-making in Congress*, Congressional Research Service, May 1984; and Louis Fisher, “Annual Authorizations: Durable Roadblocks to Biennial Budgeting,” *Public Budgeting and Finance*, Spring 1983.

<sup>9</sup> Schick, *Legislation, Appropriations, and Budgets*, p. 8.

<sup>10</sup> The House Appropriations Committee was established in 1865; the Senate Appropriations Committee was established in 1867. The events leading to the establishment of these committees are discussed in Charles H. Stewart III, *Budget Reform Politics: The Design of the Appropriations Process in the House of Representatives, 1885-1921* (New York: Cambridge University Press, 1989), pp. 53-83; and U.S. Senate, Committee on Appropriations, *Committee on Appropriations: 1867-2008*, 110<sup>th</sup> Cong., 2<sup>nd</sup> Sess., Doc. No 14 (Washington, DC: GPO, 2008), pp. 4-6.

<sup>11</sup> Stewart, *Budget Reform Politics*, pp. 89-132.

<sup>12</sup> Background on these changes is provided in U.S. House of Representatives, Committee on Appropriations, *A Concise History of the House of Representatives Committee on Appropriations*, 111<sup>th</sup> Cong., 2<sup>nd</sup> Sess. (Washington, DC: GPO, 2010), pp. 7-11; U.S. Senate, Committee on Appropriations, *Committee on Appropriations: 1867-2008*, pp. 9-16.

activities. At about the same time, appropriations, which used to be comprised almost entirely of specific line items, shifted to more general lump sums for purposes that were usually identified simply by referencing the statutory authorization. In other words, appropriations began to rely on the authorization statutes to specify and limit how the funds would be used.

Coincident with the enactment of the Budget and Accounting Act of 1921, the reconsolidation of Appropriations Committee jurisdiction over general appropriations increased the committee's role in congressional decisions about spending. In response, the legislative committees began to explore new legislative language that would influence budgetary outcomes both with respect to the action of the appropriators and also in their oversight of the agencies under their jurisdiction. This resulted in significant changes in the content and timing of authorization laws over the next several decades.

### Emergence of Explicit Authorizations of Appropriations

The first significant change in the form of authorization laws occurred after the 1920s, when authorizations began to include provisions that explicitly authorized future appropriations tied to certain purposes. At a minimum, such provisions were a recommendation of the legislative committees as to the level of future appropriations. This practice, however, had broader implications for the role of the legislative committees in budgetary decisionmaking, because the existing House and Senate rules that prohibited appropriations not authorized by law had to be applied in new ways. Although these prohibitions were longstanding, having been first adopted during the previous century, authorization provisions that established an entity, project, or activity had been considered sufficient to implicitly authorize subsequent appropriations under the terms of those rules. However, when the legislative committees started to include explicit provisions authorizing appropriations, this effectively enabled them to create procedural ceilings on subsequent appropriations and thus exert greater influence over subsequent funding decisions.<sup>13</sup>

As language specifically authorizing appropriations was increasingly used, various practices started to emerge. First, the legislative committees began to authorize definite amounts to be appropriated for specific fiscal years. In their early use, such provisions were usually tied to minor or temporary programs. Because provisions that limited the amount or duration of future appropriations were considered to be inappropriate for permanent or large-scale government programs, language authorizing appropriations for "such sums as are necessary" were typically used for such programs. Over the postwar period, however, as these committees continued to increase their use of such language, they began to apply it to programs of a more large-scale or permanent nature. Second, the legislative committees began to conduct reviews (associated with the expiration of these provisions) and enact revisions to authorization laws for certain agencies and departments on periodic schedules instead of on an as-needed basis. While the timing of these revisions was to coincide with the need to reauthorize appropriations, these revisions also provided an occasion to make needed programmatic changes.

The types of provisions periodically authorizing appropriations that were developed during this period have continued to be used through the present day. These provisions generally indicate two schedules of legislative review: "annual" and "multiyear." *Annual* authorizations of appropriations explicitly authorize appropriations for a single fiscal year. *Multiyear* authorizations of appropriations explicitly authorize appropriations for more than one fiscal year at a time (typically between two and five).

<sup>13</sup> The legislative committees also employed other mechanisms during this period to influence fiscal decisionmaking, such as so-called "backdoor spending," which included borrowing authority, contract authority, mandatory entitlements, and permanent appropriations. For a further discussion of these and other such mechanisms, see Louis Fisher, "The Authorization-Appropriation Process in Congress: Formal Rules and Informal Practices," *Catholic University Law Review*, vol. 29 (1979-1980), pp. 51-105.

Although the proportion of agencies and programs that were subject to annual or multiyear reauthorizations expanded significantly during the mid-20<sup>th</sup> century, variation has continued in approach and congressional practice. Many agencies and programs are still authorized on a permanent basis, and others have been subject to different reauthorizations schedules at different times.<sup>14</sup> In addition, because an agency is often subject to a patchwork of authorization laws that have been enacted over the course of its existence, that agency may experience a variety of authorization schedules and approaches simultaneously. Finally, in an increasing number of instances, annual or multiyear authorizations of appropriations have lapsed or have not been renewed in a timely manner for a variety of potential reasons.<sup>15</sup> For example, a lapsed authorization of appropriations could be due to the authorizing committee's assessment that no programmatic changes are currently needed. Alternatively, it could indicate a lack of congressional support for the program's continuing existence or obstacles to achieving congressional consensus regarding the programmatic changes that would be part of the debate on reauthorization. This multiplicity of reasons presents a challenge when Congress attempts to assess what expired authorizations of appropriations mean in a given context, especially when the primary procedural avenue to address them is part of the appropriations process.

### House and Senate Approaches to Appropriations Not Authorized by Law

As the congressional rules and practices related to authorizations and appropriations have evolved over the years, so has the meaning of the phrase "authorized by law" as it is interpreted and applied in each of the chambers to the general appropriations measures that it considers.<sup>16</sup> In a number of respects, the House and Senate have developed divergent rules related to this issue, although their approaches diverge to a lesser extent in practice.

One area of difference between House and Senate rules is under what circumstances appropriations not authorized by law are prohibited. The House restriction in Rule XXI(2)(a)(1) broadly applies to provisions in any general appropriations bill or amendment thereto. However, in current practice, the House almost always waives points of order against provisions in the bill for failure to comply with Rule XXI(2) through the special rule<sup>17</sup> that provides for the measure's consideration.<sup>18</sup> As a consequence, when

<sup>14</sup> For a discussion of this variety of approaches and illustrative case studies, see CRS Report R43862, *Changes in the Purposes and Frequency of Authorizations of Appropriations*, by Jessica Tollestrup.

<sup>15</sup> The Congressional Budget Office (CBO) is required to compile this information each year under Section 202(e)(3) of the Congressional Budget Act. For FY1988, CBO identified a total of 45 laws with expired authorizations of appropriations (CBO, *Report on Unauthorized Appropriations and Expiring Authorizations*, January 15, 1988). That total grew to 256 such laws for FY2016 (CBO, *Unauthorized Appropriations and Expiring Authorizations*, January 15, 2016).

<sup>16</sup> Both the House and Senate restrictions apply to general appropriations bills, but the chambers define such bills differently. In the House, "general appropriations bills" are the annual appropriations acts (or any combination thereof) and any supplemental appropriations acts that cover more than one agency. Continuing resolutions are not considered to be general appropriations bills (*House Practice*, ch. 4, §3). In the Senate, "general appropriations bills" are the annual appropriations acts (or any combination thereof) and any supplemental or continuing appropriations acts that cover more than one agency or purpose (Floyd M. Riddick and Alan S. Frumin, *Riddick's Senate Procedure: Precedents and Practices*, 101<sup>st</sup> Cong., 2<sup>nd</sup> sess., S. Doc. 101-28 [Washington, DC: GPO, 1992], p. 159).

<sup>17</sup> Special rules are simple resolutions reported by House Rules Committee that set the terms for considering a measure and are effective once adopted by the House. The Rules Committee has exclusive jurisdiction over special rules. For further information, see CRS Report 98-433, *Special Rules and Waivers of House Rules*, by Megan S. Lynch.

<sup>18</sup> This practice dates back to about the 80<sup>th</sup> Congress (1947-1948). For further background, see U.S. Congress, House Committee on Rules, *A History of the Committee on Rules: 1st to 97th Congresses*, committee print, 97th Cong., 2nd Sess., (Washington, DC: GPO, 1983), pp. 156-159; Stanley Bach, "From Special Orders to Special Rules: Pictures of House Procedures in Transition," paper presented at the American Political Science Association annual meeting, San Francisco, CA, 1990, pp. 28-29; Stanley Bach, "Representatives and Committees on the Floor: Amendments to Appropriations Bills in the House of Representatives, 1963-1982," *Congress and the Presidency*, vol. 13, no. 1 (Spring 1986), pp. 43-44.

the House is considering an appropriations measure, Rule XXI(2) in practice primarily limits the content of floor amendments.<sup>19</sup>

The Senate prohibition in Rule XVI(1) is comparatively more narrow than the House, even in light of the House practices discussed above. Because it is framed in terms of amendments that would increase the amount for an item in the bill or add a new item, it does not apply to House-passed language, measures originated by the Senate Appropriations Committee, amendments to a House-passed bill reported by that committee, or amendments offered by direction of the authorizing committee with relevant jurisdiction, which have been reported and referred to the Appropriations Committee at least one day before consideration.<sup>20</sup> In other words, the Senate prohibition applies primarily to amendments offered by individual Senators during floor consideration of general appropriations bills. There is no opportunity to raise a point of order under Rule XVI(1) against an unauthorized appropriation in the bill itself or an Appropriations Committee amendment to that bill.

A second area of difference is the timing of when a program or activity may be considered authorized by law. In the House, Rule XXI(2)(a)(1) requires that an authorization be *enacted* prior to consideration of the relevant general appropriations bill in order for its appropriation to be considered authorized.<sup>21</sup> In the Senate, Rule XVI(1) requires an authorization only to have been *passed* by the Senate during the current session of Congress prior to consideration of the relevant general appropriations bill in order to be considered authorized.<sup>22</sup> This broad Senate criterion under which an appropriation may be considered to be authorized also more narrowly defines the circumstances under which a point of order could be raised compared to the House.

A third area of difference is the types of projects and activities for which the rules provide an exception and thereby allow funds to be appropriated in the absence of being authorized by law. For example, House Rule XXI(2)(a)(1) contains a provision that excepts appropriations that would continue “public works and objects already in progress” from the prohibition on unauthorized appropriations. The Senate has no such exception. Senate Rule XVI(1), however, allows appropriations for projects and activities “proposed in pursuance of an estimate submitted in accordance with law.”<sup>23</sup> Such estimates can be provided in the President’s annual budget request, as required by 31 U.S.C. 1105(a) and 1107, or through deficiency and supplemental appropriations requests made after the President’s budget request has been submitted to Congress.<sup>24</sup> The House has no such exception.

Setting aside these areas of difference, however, both chambers’ rules in modern practice seek to encourage the timely enactment of authorizations through consequences that would be felt in the appropriations process. One challenge of approaching the issue of expired authorizations from this

<sup>19</sup> On some occasions, the waiver for the bill provided by the special rule leaves specified provisions unprotected. In many such instances, the Rules Committee chooses to do so because the authorizing committee of jurisdiction objects to the inclusion of a particular unauthorized appropriation (or legislative provision). This practice has generally been recognized as the “Army Protocol” since the 104th Congress. During subsequent floor consideration of that appropriations measure, if a point of order under Rule XXI(2) were raised against an unprotect provision and sustained, that provision would be stricken and consideration of the bill would continue. For further information, see House Rules Committee, “Open Rules and Appropriations Bills,” May 1, 2009, <http://rules-republicans.house.gov/Media/PDF/BT-OpenRules.pdf>; Walter Oleszek, *Congressional Procedures and the Policy Process* (Washington, DC: CQ Press, 2007), 7<sup>th</sup> ed., pp. 134-135; and *House Manual, One Hundred Fourteenth Congress*, H.Doc. 113-181, 113<sup>th</sup> Cong., 2<sup>nd</sup> sess., [compiled by] Thomas J. Wickham, Parliamentarian (Washington: GPO, 2015), §1044, p. 850.

<sup>20</sup> *Riddick’s Senate Procedure*, pp. 171, 189.

<sup>21</sup> See *House Practice*, ch. 4, §10, for a further discussion of this requirement.

<sup>22</sup> *Riddick’s Senate Procedure*, p. 187.

<sup>23</sup> *Ibid.*, p. 180.

<sup>24</sup> *Ibid.*, p. 155.

perspective, however, is that these required authorization actions are not within the control of the Appropriations Committees. In addition, this framework can effectively set up a choice between, on the one hand, delayed appropriations for programs or activities that agencies may still be required to undertake or, on the other hand, funding unauthorized programs. As a result, this mechanism's effectiveness is limited when appropriations are unauthorized for reasons that are not directly related to whether that purpose should continue to receive funding.

Attempting to address the issue of expired authorizations through the authorization process, however, has its own challenges. Neither the Senate nor the House has rules that govern the form of authorizations. In addition, the responsibility for authorizations is decentralized and divided by subject matter jurisdiction among a number of committees. The different approaches to authorization that these committees take may be the result of a number of factors, including conscious choices driven by the current needs of the program, historical practices adopted at the time the authorization was first enacted, and current legislative challenges and opportunities. The flexibility in approach that chamber rules allows can enable the authorization process in a particular instance to be adapted to the committee's requirements related to agency oversight and the committee's desired role in congressional budgetary decisionmaking. The challenge posted by this flexibility is that the resultant lack of standardization can make addressing expired authorizations on a widespread basis more difficult.

Chairman ENZI. It will be. Thank you.  
Dr. Posner.

**STATEMENT OF PAUL L. POSNER, PH.D., DIRECTOR OF GRADUATE PUBLIC ADMINISTRATION PROGRAM, AND CENTER ON THE PUBLIC SERVICE, SCHOOL OF POLICY, GOVERNMENT AND INTERNATIONAL AFFAIRS, GEORGE MASON UNIVERSITY**

Mr. POSNER. Thank you, Mr. Chairman and Senator Whitehouse. I appreciate your hearing today. I think this is a very important issue, and it is something that usually is not the primary topic on the evening news, but oversight is important. And it is important to institutionalize it more than we are doing.

There is no question that the budget process is broken. There is a consensus on that. I am co-chairing a National Budgeting Roundtable with Stuart Butler, Maya MacGuineas, and people like Alice Rivlin and Rudy Penner and other long experts in the budget process, and we all have agreed on one thing: that the budget process has largely failed to meet the broad vision that was created in 1974. And among those things was the fact that budgeting would be more than just setting a top-line number for appropriators, that the budget process would provide Congress with a vehicle to take a holistic look at the budget and rank relative priorities across competing claims. As one Budget Director said, the point of budgeting is not to go after weak claimants but to go after weak claims. And the budget process is a vehicle to potentially do that.

We have seen—and I do not need to repeat—how the budget process itself has disintegrated in the face of gridlock and polarization. There are tremendous limits on the kinds of tradeoffs that can happen across these walls we have created between discretionary, mandatory, tax expenditures and the like. And Congress does not have the vehicle to take a holistic look, a comprehensive look at broad areas of policymaking, whether it is low-income housing, higher education assistance, drug policy, or food safety.

So I think this is an important issue, and I am glad you brought it up and raised it to the level of a hearing. And I agree that unauthorized programs are an issue, and they are symptomatic of the same fragmentation and gridlock that has afflicted the broader budget process. I think it really inhibits the Congress' capacity to budget and ability to budget.

Ideally, you would like to have oversight of broad programs from many perspectives. The appropriations have one that is focused on finance and line items in some cases. The program experts are in the authorizing committees, and you need to have them weigh in periodically. If they are not, I think it is a limit to our process. And as I will say in a minute, the Budget Committees are the one Committee that has been largely missing in action in the oversight project, and I am going to suggest an opportunity there for the Budget Committees themselves.

As much as we all will decry the kind of lapsing reauthorizations and the like, fixing the problem is another issue itself. As was said earlier, the authorization process is highly decentralized. The reasons for lapsed reauthorizations have something to do with gridlock and something to do with a lot of other idiosyncratic effects. De-

signing one-size-fits-all reforms are difficult in this environment, and it requires, I think, possibly the adoption of somewhat of a pilot process where this Committee perhaps works with authorizers and appropriators on a policy area to phase in a new set of incentives to encourage authorizers to come more to the table on this. We can talk about that later, but I think that may be the way to go here.

Most importantly, the notion of program-by-program authorization, while it is something we all can agree on, is really not in sync with how the Federal Government impacts broad outcomes. Basically, the actions of individual programs are really not as important as the actions of groups of programs combined, what I call “portfolios of programs.” So if we look at higher education or we look at food safety or we look at low-income housing, we can examine in depth down to the level of the lowest provider the impact of each program. But to really get a sense of what impact the Federal Government is doing, you have to look at them together in some way. You have to look at what I call the “portfolio of Federal programs,” not only the spending side, not only mandatories and discretionaries, but tax expenditures.

In low-income housing, for example, the low-income housing tax credit is the largest Federal spending program in housing, and yet it is completely off the table in all of the things that the agencies do. HUD takes no ownership of it, for example, and, frankly, neither does the IRS.

The Budget Committees were set up to look holistically through a series of budget functions and subfunctions that you use to craft the budget resolution, but then they are completely forgotten. I am suggesting in the testimony that we need to resurrect that. I have illustrated how that can work in higher education where we could take a holistic look across tax and spending, and look at the synergies and the disconnects between the programs across the board. This Committee has an opportunity to be the steward of that process, recognizing that is not the easy thing to do, as Senator Whitehouse said. This Committee does not have the power and the leverage. I think we really need to rethink the role of this Committee and the composition of this Committee, and if we are going to have this Committee fulfill what I consider its oversight role to be the steward of the cross-cutting programs of Government, we need to think about this Committee becoming more of a leadership committee and stocking it with the key leaders of the various committees. This Committee then would be in a position to drive policy change and oversight in a real meaningful way.

[The prepared statement of Mr. Posner follows:]

**Can We Institutionalize More Comprehensive Oversight in Federal Budgeting?**

**Statement of Dr. Paul L. Posner,  
Director of Graduate Public Administration Program  
School of Policy, Government and International Affairs  
George Mason University**

**For  
"Spending on Unauthorized Programs"  
Hearing before  
The Committee on the Budget  
United States Senate  
Wednesday, February 3, 2016**



**Statement of Paul L. Posner**

Chairman Enzi, Ranking Member Sanders and other Members of the Committee,

I want to thank you for inviting me to share my thoughts with you on Congressional budget reform. I commend the Committee for taking on this important and challenging project. The growth of unauthorized programs that is highlighted today is one manifestation of the challenges Congress faces in keeping up with oversight and updating of funding authorizations at a time of polarization and gridlock.

It goes without saying that these same trends have significantly hampered the capacity to budget in the Congress. Looking back to the Congressional Budget Act of 1974, the process largely succeeded in addressing one problem by rebalancing power between the President and Congress. Armed with its own highly credible budget office, Congress became a contestant in an annual battle for fiscal position and positioning. However, since that time, the budget process has become embroiled in polarized politics, barely able to keep the government open and financed. When it does achieve this very minimalist goal, it does little beyond providing an allowance for discretionary appropriations. And these ceilings have become increasingly symbolic statements rather than politically realistic targets to guide appropriations decisions. Budgeting has become less an arena to solve fiscal and policy problems together and more of a staging area where positions are taken for primary constituencies and other audiences far removed from running the government.

The challenge you face is how to reimagine a budget process that can enable the Congress to achieve three important objectives: (1) set fiscal policy likely to keep the nation's economy on a sustainable course, both for today and the longer term; (2) allocate resources to assure that scarce resources are used to support the highest priorities; and (3) ensure that government is equipped to deliver public

services in the most efficient and effective way possible. I am well aware that the venture you have undertaken has to not only satisfy public policy objectives, but also must ensure that whatever process reforms are proposed gain sufficient political support.

I would add that you aren't alone in this venture. A number of veterans of the budget process have been working over the past year through a National Budgeting Roundtable co-chaired by Stuart Butler, now of the Brookings Institution, Maya MacGuinness, President of the Committee for a Responsible Federal Budget, and myself. With seasoned former officials like Alice Rivlin and Rudy Penner, we collectively launched a multi-year effort supported by the William and Flora Hewlett Foundation designed to bring in new ideas from academic fields like political science and behavioral economics as well as experiences of other nations struggling with fiscal challenges. My testimony draws from some of the papers and briefing sessions we have held so far.

#### **Allocating scarce resources: the inescapable challenge for budgeting**

In my testimony today, I will address how we might improve our capacity to make tradeoffs among competing claims for limited resources. Budgeting is centrally about how to make hard choices. Unlike other policy areas like social security or criminal justice, we have to make these choices every year. As we have learned, failure to do so comes with the high price of shutting down the government.

Ideally, a budget process should facilitate informed tradeoffs among competing objectives, programs and tools of government. Former Congressman Charles Stenholm best described the competition that the congressional budget process was intended to inspire: "This process will require many tough choices as priorities are set among worthy programs. But essentially, all programs will be together in the same boat, competing for priority status as we seek to determine how best to allocate the revenues coming into the U.S. Treasury."

I am concerned that the congressional budget process has strayed far from the vision of Mr. Stenholm and other guardians of the fiscal commons. The tradeoffs and hard choices that budgeting requires are far more difficult to achieve under our current political system than the one we had when the Congressional Budget Act was passed in 1974. The virtual fish bowl of media and interest group coverage makes forming coalitions and winning necessary concessions far more difficult and even politically hazardous for members and presidents alike. The disappearing middle in Washington removed the ballast that is often so essential to bring about fiscal order from the political cacophony that is Washington today.

The disintegration of budgetary norms and processes has left us with these legacies:

--**Delays and stalemates** - Congress has failed to adopt a budget resolution nine times since the 1974 Act. We have largely been operating government on temporary continuing resolutions for most years since the 1970's. The GAO issued a report on the costs of the debt limit for the economy, noting that the uncertainty associated with the 2013 debt limit passage increased federal borrowing costs as borrowers avoided affected Treasury securities, raising their rates.<sup>1</sup> Simply put, the budget process has been unable to insulate itself from the rising levels of polarization that have gripped the nation at all levels of government. Thus, the failure to budget has become a metaphor for the underlying national disenchantment with government itself.

--**Slippage in implementation of Congressional budget goals** - The Congressional budget process built in a tension between the whole and the parts of budgeting. Like the public they serve, Congress often reflects ambivalence between its support for broad fiscal constraints and its support for many of the spending and revenue programs of the government. Thus, for instance, discretionary spending ceilings in

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<sup>1</sup> Government Accountability Office, *Debt Limit: Market Response to Recent Impasse Underscores Need to Consider Alternative Approaches*, GAO-15-476, July, 2015.

the budget resolution lose their appeal when translated to specific appropriations cuts and other actions. The result is either the failure to pass appropriations bills under regular order or the use of “gimmicks” to sidestep the constraints. The expansive use of emergency spending can provide room beyond the caps for certain discretionary spending, while exemption of certain legislation from the PAYGO scorecard enables new mandatory programs to increase deficits.<sup>2</sup>

--**The asymmetrical focus on discretionary spending** in the budget process. This part of the budget often bears the disproportionate impact of fiscal targets and constraints, while existing tax and spending entitlements continue to drift upward with no regular review and little or no limits. Discretionary spending has declined from 9.3 percent of GDP when the Budget Act was passed in 1974 to less than 7 percent today, while mandatory programs have doubled during the same period to 13.5 percent of GDP. Tax expenditures, which function much like spending programs, are estimated at 8 percent of GDP, exceeding discretionary spending, and yet escape regular review. Deficit reduction plans can achieve greater savings in a more balanced way if they are applied against a broader base including spending and tax entitlements. While cutbacks are never easy, they are likely to be perceived as more fair if levied against all claims in the budget affecting all major stakeholders. Fiscal history tells us that stakeholders are not likely to accept the legitimacy of cuts if they are singled out, raising fears that their sacrifice will be exploited by champions of other budgetary claims.

--**Limits on policy tradeoffs** – the current budget process is highly balkanized, with high walls separating programs in discretionary, mandatory and tax expenditure sectors. Related programs for such federal policies as higher education assistance or low-income housing are splintered across this fragmented budgetary landscape. While the budget resolution discusses the 19 budget functions that provide a mission oriented framework integrating related programs across the budget, these

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<sup>2</sup> See Committee for a Responsible Federal Budget, *The Better Budget Process Initiative: Strengthening Statutory Budget Enforcement*, June 25, 2015.

potentially helpful categories are not, in fact, used to prompt appropriators or authorizers to consider how to allocate scarce resources across these competing programs. The inventory of duplicative and overlapping programs compiled periodically by GAO is one reflection of rampant fragmentation across the federal landscape in programs addressing common goals.<sup>3</sup>

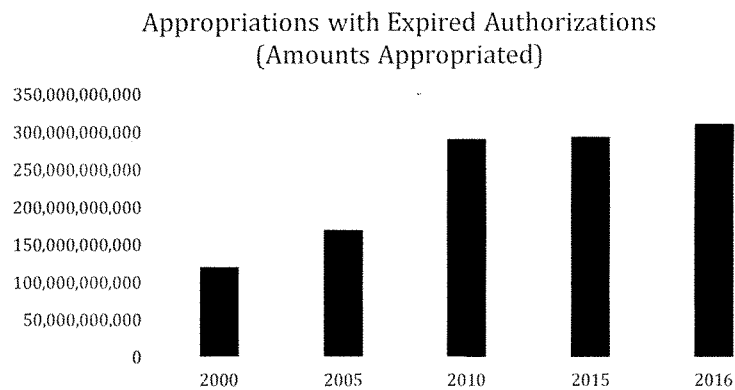
### **The Eclipse of Funding Authorizations**

The growth of discretionary spending with expired authorizations has been chronicled in reports by CBO over many years.<sup>4</sup> It is instructive to examine the trends reported over time. The following chart shows the trends in expired authorizations funded in appropriations since 2000.

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<sup>3</sup> Government Accountability Office, *2015 Annual Report: Additional Opportunities to Reduce Fragmentation, Overlap and Duplication and Achieve Other Financial Benefits*, GAO-15-404SP, April 2015

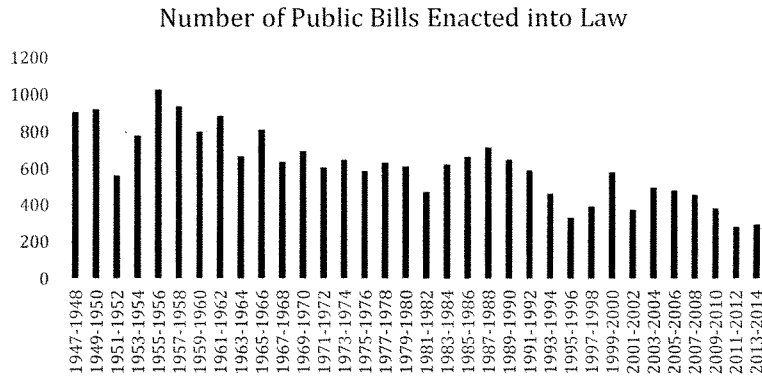
<sup>4</sup> The Congressional Research Service has suggested that even when the specific authorization of appropriations expires, some programs and agencies may still be regarded as authorized if they retain underlying statutory authorization for the program. Jessica Tollestrup and Brian T. Yeh, *Authorization of Appropriations: Procedural and Legal Issues* (Washington, CRS, September 9, 2014)

**Figure 1**

There are many reasons for this trend, but this undoubtedly reflects the increasing polarization of the Congress itself. Simply put, it is more and more daunting for authorizing committees to contemplate taking legislation to the floor in a Congress where legislation that once garnered large majorities is increasingly at risk of being trapped by partisan gridlock, reinforced by the expanded use of filibusters and other procedural obstacles. Indeed, studies show that there has been a long term decline in the enactment of public laws over the past 60 years.<sup>5</sup>

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<sup>5</sup> See Jacob R. Straus, "Comparing Modern Congresses: Can Productivity be Measured?" in Congressional Research Service, *The Evolving Congress*, report prepared for the Senate Committee on Rules and Administration, December, 2014, pp. 217-245



Trends in the congressional budget process itself may also be responsible for this trend. At one time, authorizers were eager to pass authorizations of appropriations as a signaling device to influence appropriators. However, the advent of discretionary caps meant that appropriations were increasingly driven by overall 302(a) and 302(b) limits established in budget resolutions and by the appropriations committees.

I share the view that the role of authorizing committees in periodically renewing and reviewing programs is healthy for the budget and for public policy in general. Studies have shown that finite authorizations have prompted committees to engage in a much needed periodic updating of legislation and priorities.<sup>6</sup> Moreover, authorization terms prompted committees to schedule oversight hearings geared to the planned expiration of programs. By doing this, Congress creates a schedule for when a given policy will be considered and systematically steers the management of public programs by changing the resources and tools available to policy implementers. Whether it be periodic surface transportation, farm or higher education programs, the defined authorization period served the purpose of

<sup>6</sup> Thad Hall, *Authorizing Policy* (Columbus, Ohio: Ohio State University Press, October 2004).

sustaining the relevance of authorizers as a central policymaking and review institution for the Congress.

Finding an institutional fix to reinstitute the incentives for authorizing committees to reauthorize appropriations, however, is no simple matter. As Toelstrup says, the responsibility for authorizations is decentralized in both House and Senate. Each committee makes idiosyncratic choices driven by funding history, legislative challenges and changes in the environment.<sup>7</sup> The failure to reauthorize funding provisions may be related to problems gaining a majority for changes, or it may reflect a consensus that the committee does not feel further changes are necessary. Even though the explicit funding provision may not be updated, the underlying organic enabling statute typically remains in effect. Stronger restrictions on considering unauthorized appropriations could very well be considered. While this could prompt additional hearings and oversight, it may lead to a backlog of programs that fail to pass through the polarized gauntlet that Congress has become. This could either inspire further ad hoc efforts to include unauthorized provisions in appropriations or inspire authorizers to seek permanent funding authorizations that do not expire or require subsequent committee review. Given the fact that authorizations have diminishing influence on cap constrained appropriators in any case, a stronger provision could, in effect, prompt Congressional authorizers to walk back from finite authorizations of appropriations.

### **The Role of the Budget Process**

While much of the responsibility for resource allocation and program review rests rightly on the shoulders of authorizers and appropriators, the congressional budget process itself has largely been missing in action when it comes to oversight, program review and reallocation. The Budget Committee indeed has broader

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<sup>7</sup> Jessica Toelstrup, “Spending on Unauthorized Programs”, statement before the U.S. Senate Committee on the Budget, February 3, 2016.



perspectives that are important, and different from those of the authorization and appropriations committees.

The most recent CBO baseline report illustrated that the federal budget is on a deficit trajectory, with rising debt to GDP ratios over the longer horizon. While spirited disagreement abounds on what the nation's fiscal policy should be, these figures suggest that fiscal policy conflicts and concerns will preoccupy the congressional budget process for years to come. As Congress struggles to address fiscal issues, the budget process should not only set a single number for discretionary spending, but should provide guidance to other committees of Congress about how to consider priorities across programs and tools.

As we think about priorities for using resources, it has become more apparent that the important goals and objectives of policy cut across the narrow confines of programs, budget accounts, bureaus, and congressional committees. For instance, nearly one half of the budget authority for homeland security is provided by numerous agencies outside the Department of Homeland Security. Indeed, most of the major missions of government transcend the boundaries of the federal government itself, requiring partnerships with state and local governments, nonprofit organizations and private for profit firms. GAO's work points to systemic fragmentation and overlap across government agencies and programs serving common objectives.

A performance assessment process may help lay the groundwork for making choices that not only address macro fiscal goals but also promote improved performance by reexamining existing program commitments. Ideally, such a process would consider the entire portfolio of federal programs and activities addressing similar goals and outcomes, including mandatory and discretionary spending as well as tax expenditures. It would take advantage of the information on goals and performance Congress mandated be developed when it passed the Government

Performance and Results Act Modernization Act, and take advantage of the Act's requirements for consultation with Congress when policy objectives are established.

This kind of necessary, but all-too-rare cross cutting review and reexamination generally does not take place within the confines of appropriations or authorizing committees. Rather, the budget committees were established precisely to lead and coordinate crosscutting assessments of budgetary choices. The Budget Committee not only has a government-wide perspective, but also uses budget functions as building blocks for the budget resolution. Functions and subfunctions serve as proxies for broad missions or goals that can be the foundation for systematic performance assessments of the myriad of programs and tools addressing each mission. Moreover, the annual budget focus gives these Committees a routine responsibility that can be coupled to the process for setting policy goals and assessing performance in relation to those goals.

#### **A Portfolio Approach to Reexamining the Base**

The process that is well suited to the Budget Committee's unique perspective and scope is a portfolio budget review. Most federal policy objectives are supported by a portfolio of funding tools and programs cutting across both executive agencies and committee jurisdictions. Such a review would examine all programs related to a common budget subfunction or objective, whether they be funded through discretionary spending, mandatory programs or tax expenditures. Established congressional institutional and budget practices make it harder than necessary to trade off between related discretionary spending, mandatory programs and related tax expenditures that all contribute to funding higher education, child care, job training, low income housing, and research and development. A process that was organized by goals and associated spending and tax expenditure portfolios would review older claims and programs to either reduce the deficit or to free up resources to fund emerging priorities and programs.

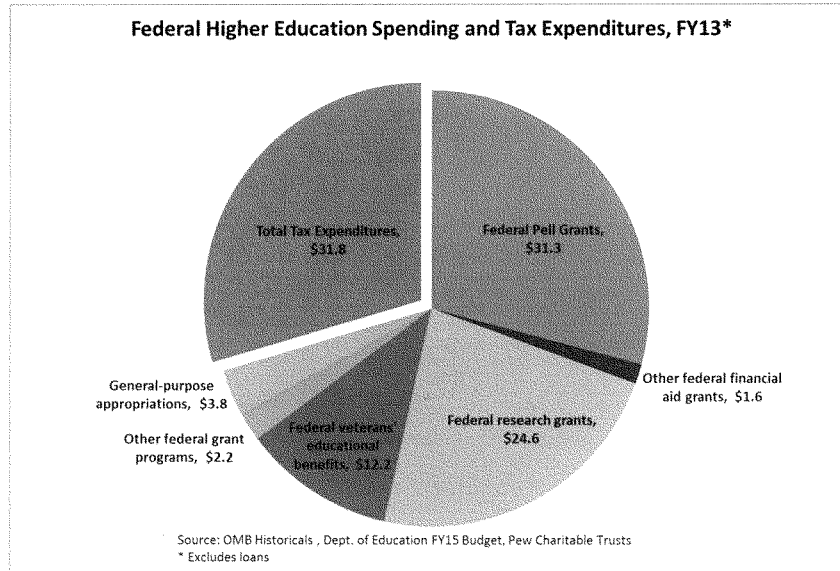
Most nations in the OECD now use a comprehensive spending review process to periodically consider broader policy areas in the budget process. Many nations have learned from the Netherlands, which has been doing these reviews for at least twenty years. The 2010 spending review examined 20 topics and was designed to produce options to reduce spending by 20 percent over four years. So-called Interdepartmental Spending Reviews have been ongoing since the early 1980's, featuring a review of policy arenas that cut across ministries. These initiatives have often included not only Finance and line ministry staff but also outside experts and have led to significant savings over the years.<sup>8</sup>

My colleague, Steve Redburn, and I have developed a paper applying portfolio budgeting to the area of federal aid for higher education.<sup>9</sup> The federal budget provides an array of separate grant and loan programs and tax expenditures to help students pay for college, including special programs for veterans. The chart below shows the composition of federal activity - federal spending for higher education will exceed \$75 billion, slightly more than the States are expected to spend for their public higher education institutions, with an additional \$30 billion of tax expenditures provided through eleven discrete programs in the tax code. These figures do not include federal loans, which now have a total volume of \$700 billion, even though such programs turn a profit annually for the federal budget.

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<sup>8</sup> OECD, *Reallocation: The Role of Budget Institutions* 2003

<sup>9</sup> Steven Redburn and Paul Posner, *Portfolio Budgeting: How a New Approach to Resource Allocation Could Yield Better Decisions*, Washington, National Budget Roundtable, July, 2015



While federal aid has grown, the myriad of subsidies has not been considered holistically, but rather has grown up in an ad hoc fashion, incubated in different congressional committees and federal agencies. It is ripe for review. In many ways, U.S. higher education is the envy of the world. At the same time, many questions have been raised about how effectively the current system of federal grants and loans is contributing to access by those who otherwise would not attend college and whether the increasing reliance on debt is reducing the personal economic returns that otherwise would accrue to those receiving federal support. Questions have been raised about whether federal subsidies are incentivizing states to reduce their own aid for students and inducing universities to raise tuition. Other questions revolve around whether the range of options and interactions among student loan

and grant programs make them hard to understand and challenging for students to calculate how best, when, and where to use them.<sup>10</sup>

The selection of areas for review and performance improvements could be accomplished in the Congress either by the leadership in consultation with the President or by this Committee as a part of the congressional budget process. The existing budget functions and subfunctions could be used as a basis for determining crosscutting policy areas, as intended when they were folded into the congressional budget process.

The budget committees can take the lead in fostering broad based portfolio reviews of major functions or subfunctions. They can do this on their own through task forces, similar to performance based reviews done by task forces of the Senate Budget Committee in the previous decade. The Budget Committee can also do this by working through authorizing and appropriations committees, commissioning portfolio reviews in concert with these committees. Such reviews can be triggered by reconciliation instructions, with committees expected to report savings to be integrated by the budget committees in a reconciliation bill. Alternatively, the authorizing committees themselves could make decisions about which areas are ripe for portfolio reviews through the views and estimates process.

The Executive Branch could be engaged in a collaborative effort to undertake a series of selective portfolio reviews. The President and Congress could reach agreement about those areas to be assessed in each budget year. Congress could help ensure that areas that are ripe for reexamination, such as those up for reauthorization, would get attention in the executive review process. Such a process would require the Congress to articulate its oversight and reexamination priorities

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<sup>10</sup> U.S. Government Accountability Office, *Student Aid and Postsecondary Tax Preferences: Limited Research Exists on Effectiveness of Tools to Assist Students and Families Through Title IV and Tax Preferences* GAO-05-684, July, 2005

centrally and the President to invite Congress to help determine priorities to guide the executive program assessment process.

I don't need to tell this Committee that the performance assessment process I am suggesting will not be easy. There is no low hanging fruit in the federal budget. In fact, performance based assessments of the base of groups of programs will entail the prospect of greater conflict. This new role will require the Committee to gain the support of other leaders in the Congress as well as the Administration. It will be important for this process to be highly selective in its reviews, to avoid being overwhelmed by the sheer amount of work as well as the likely political reaction. Nonetheless, the potential rewards are substantial. Performance assessments carry the promise of transforming the budget process into a more strategic and forward looking vehicle for setting the nation's priorities.

#### **Conclusion: Transforming the Budget Committees**

Budget process reforms present risks and opportunities for the Congress and this Committee. The agenda for budget process reform I have laid out would place new demands on the federal budget process in general and this Committee in particular. I am well aware that these emerging roles are even more challenging for a budget process that has trouble simply passing a budget resolution and securing a full year's appropriations for the agencies. Yet the fiscal challenges and the need to update our priorities both call for major new activities and functions that can best be performed by the Budget Committees.

Strengthening Congress' capacity to budget will call for stronger leadership within the Congress and from the President as well. This Committee will be challenged to assert a more proactive role in setting priorities, reviewing government performance and shifting how we budget for the long term. This is a tall order, particularly during a period of polarization that has come to define today's politics.

It may be time to rethink the nature of the budget committees. Established in 1974 as new committees alongside an established committee structure, the budget committees have increasingly been tasked to take on government-wide leadership without sufficient influence over other committees to do the job. Accordingly, some have suggested that budget committees be transformed into leadership committees, comprised of the chairs of the major committees of each house.<sup>11</sup>

An old adage in management suggests that form should follow function. The original design of the 1974 Budget Act contemplated a less ambitious role for the budget committees. Powerful committees were at hand to trim their sails, Yet over time, the budget process has had to adapt to serve new functions – reconciliation, new scoring rules implementing new budget legislation and greater demand for more complex analysis of long term and dynamic economic effects of proposed legislation have all changed the scope and stakes of the congressional budget process. The Budget Committees are at a threshold moment and need to adapt to meet the emerging needs of the Congress and the nation for a revitalized budget process.

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<sup>11</sup> Philip G. Joyce, “Strengthening the Budget Committees: Institutional Reforms to Promote Fiscally Responsible Budgeting in Congress”, paper prepared for the Federal Budget Reform Initiative, Pew Charitable Trusts, January, 2011.

Chairman ENZI. Thank you.  
Dr. Thurber.

**STATEMENT OF JAMES A. THURBER, PH.D., UNIVERSITY DISTINGUISHED PROFESSOR OF GOVERNMENT, FOUNDER AND DIRECTOR, CENTER FOR CONGRESSIONAL AND PRESIDENTIAL STUDIES, SCHOOL OF PUBLIC AFFAIRS, AMERICAN UNIVERSITY**

Mr. THURBER. Thank you for having me here today, Mr. Chair and members of the Committee. This is the first hearing that I know of on unauthorized appropriations. There have been hearings on process reform to try to improve the budget process, but this is very narrow and important.

The discussion today is really about how to improve the process to a great extent, and let me remind you very briefly from the legislative history what the goals were of the original act. I was working for Senator Hubert H. Humphrey in 1974, and I also worked for the temporary Select Committee to study the Senate Committee System (Stevenson-Brock Committee) that reorganized the Senate committee system in 1976. The Committee considered combining the authorization and appropriations committees. It was not very popular, but we had a hearing on proposal which was very controversial and received no support.

Let me remind you the goals in the Budget Act. The Act stated that Congress would complete appropriations, tax policy, and budget decisions in a timely and transparent fashion, to control budget deficits and debt, to limit growth of Federal spending; to improve ways priorities get set among different types of spending, defense and domestic; to set congressional fiscal policy; to improve the information and knowledge of the budget decisions, (creating CBO, which has worked); to establish a procedure to overcome Presidential impoundments, (which has worked); and to compete more effectively with the President and executive branch over the Federal budget. I think that the process has not met those goals in almost everything but impoundments and CBO.

Unauthorized appropriations, the topic of the hearing, in my opinion are a symptom of political polarization and gridlock in Congress. Changing the process will not change the will of the members nor the extreme polarization in Congress and in the Electorate.

The number of unauthorized programs that are funded and the amount of spending on them has gone up directly as polarization has increased. My new book called "American Gridlock" from Cambridge University Press, published last December, reveals that in 1974 about a third of the House and the Senate voted together. That was the common ground for governing. It is now down to 4 percent. If you change the rules in the Budget and Appropriations process, you are not going to change the incentive for Members to be polarized on the left and on the right.

What are the solutions to polarization and the inability of Congress to pass authorizations and appropriations in a timely fashion?

One is it takes time and special leadership in committees and on the floor to build consensus. We have seen that with the Defense



Authorization Act. We have seen it most recently with Senator Alexander and Senator Murray on The Every Student Succeeds Act of 2015. We have seen it with the Toxic Substance and Chemical Act that was recently passed. We have seen it with the “doc fix.” We have seen it with the transportation bill. We have seen it with the cyber information sharing bill. We have seen it with the funding of DHS.

These legislative successes take people who are willing to work in a bipartisan way in Committees. This Committee—and I wrote an article about it—at the very beginning was an incubator of comity and civility with Senators Muskie and Bellmon. For 5 years, they worked together closely and did a much better job than the House of Representatives, which was highly politicized. This Committee could do that again. Party leaders are structuring debate in recent years that promote rather than deter partisanship. As a result, the chambers are more partisan and deadlocked than at any time since 1860. We have a way to measure that in terms of Senators voting together in 1860, prior to the Civil War and now. About 4 percent of Senators voted together in 1860 and 2015. They were polarized then and now.

We need to improve lawmaking through legislative procedural reforms, return to the regular order—you have heard this often—have more deliberation, more transparency, limit restrictive rules, decision making and improve protection of the minority. Crisis drives out deliberation—that is a problem.

Congress also needs to return to the real post enactment conference committees that are transparent to the public and fair to the parties.

Also, there are too many committees and committee assignments. I looked at the number of Committee assignment by members of this Committee. On average, you all have four to five committee assignments. It is difficult to keep up with the work of all those committees and resultant subcommittees. There is duplication in committee jurisdictions. There is fragmentation. There needs to be a realignment of jurisdiction and reduction in the number of committees so you can all work more effectively.

This is summarized in my statement. We need to require members of both chambers to spend more time doing their job, less time going back to town meetings, hustling after campaign funds. Senator Tom Daschle recently said he thinks Members of the Senate spend more time fundraising than they do working in Congress. I call for other reforms in my testimony that will help the Senate do its job of authorizing and appropriating in a timely fashion. Congress needs to get back to work, to do rigorous oversight, timely authorizations, and thoughtful deliberation. The American people will be a little more supportive of the institution if these are done. You are in the cellar in terms of people thinking you are doing a good or outstanding job. It has been that way for years. I think one way to gain support from the public is to go back to the work of the Senate in a bipartisan way—it does not mean that you have to agree on everything—and move legislation in timely manner.

Thank you. I ask that my testimony be put into the record.

[The prepared statement of Mr. Thurber follows:]

Spending on Unauthorized Programs: Authorizations and Appropriations

Testimony on:  
“Spending on Unauthorized Programs”  
for a hearing before the  
Committee on the Budget  
United States Senate  
Wednesday, February 3, 2016 at 10:00 AM  
Room SD-608

Testimony by:  
Dr. James A. Thurber  
University Distinguished Professor of Government  
Director of the Center for Congressional and Presidential Studies  
School of Public Affairs  
American University  
[Thurber@american.edu](mailto:Thurber@american.edu)

Mr. Chairman and distinguished Members of the U.S. Senate Budget Committee,  
it is an honor to appear before you today on the topic of authorizations and appropriations.  
To my knowledge, there has never before been a special congressional committee

challenging unauthorized appropriations. Thank you for your invitation to this unique hearing. I plan to make a few observations at the outset about unauthorized appropriations, by my fundamental thesis is that Congress's partisan polarization is a main contributor to today's hike in unauthorized appropriations. After my remarks, I would be pleased to answer any questions you may have.

It is clear that House Rule XXI and Senate Rule XI contain restrictions on the consideration of appropriations that are unauthorized.<sup>1</sup> However, in practice whether an appropriation is unauthorized and whether it is a violation of a House or Senate Rules is determined by the Speaker of the House and the Presiding Officer of the Senate on the advice of the Office of the Parliamentarian in either chamber. Unauthorized appropriations exist and are common. There is a pattern of growth in the number of unauthorized programs and the amount of appropriated dollars for those programs. What the primary cause of this growth in the number of unauthorized programs and the increase in dollars appropriated for them against the rules of the House and Senate results from the current polarization and consequent dysfunctionality of Congress.

I have concluded that the volume of unauthorized appropriations (256 laws and \$310 billion for fiscal year 2016) is not Congress abdicating its responsibilities, but rather the fact that before the 1950s, most authorizations were permanent.<sup>2</sup> The move to shorter authorization periods was an attempt to force more oversight for federal programs. In 1985, Congress required the Congressional Budget Office (CBO) to write an annual

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<sup>1</sup> See House Rule XXI of the House Rules and Manual, H. Doc. 110-162, pp.836 and Rule XVI of the Standing Rules of the Senate, S. Doc. 110-9, pp. 11-12.

<sup>2</sup> Congressional Budget Office, *Unauthorized Appropriations and Expiring Authorizations*, January 15, 2016, Table 1, p. 4.

report about unauthorized appropriations, the purpose being “to help Congress use the early months of the year to adopt authorizing legislation that must be in place before the regular appropriations bills can be considered.”<sup>3</sup> The CBO report has not caused Congress to authorize more programs in a timely manner; it simply counts its failures. It is not that Congress has stopped its oversight responsibilities of these programs that are unauthorized. Congress is operating as it did pre-1960s, but falling short of the non-binding goals it set for itself – and then mandating a report in 1985 that reveals how far it has fallen short of these goals.

Adding some kind of enforcement provision to force Congress to authorize before appropriating would likely not work. If Congress does not want to “do its job” of reauthorizing programs using the regular order, adding consequences to inaction would be counter-productive.

Lack of reauthorizations does not mean there is zero oversight of programs; often, the authorizing committee carries out oversight hearings and reviews, requires GAO audits, and legislation may be reported without ultimately being enacted as a result of these activities.

Moreover, whether or not the authorizing committee has thoroughly reviewed the program or project, oversight is provided annually through the appropriations process. Appropriators say they review all discretionary spending very thoroughly on an annual basis and make needed revisions and mid-course corrections from time to time..

It is not controversial that Congress appropriates dollars for expired programs. It is commonly accepted practice. House and Senate leadership of both parties have

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<sup>3</sup> H. Rept. 99-433, (December 10, 1985), the conference report accompanying the Balanced Budget and Emergency Deficit Control Act of 1985, p. 114.

allowed this for many years. The legal and acceptable procedures are clear:

If an authorization of appropriations expires, Congress may still appropriate money to fund the particular program, agency or activity, as long as there is legislative history that shows that Congress intended for the programs to continue (and not terminate), or 'at least the absence of legislative history to the contrary'.<sup>4</sup>

The Government Accountability Office (GAO) has also been explicit that unauthorized programs may be funded, “. . . as a general proposition, the appropriation of funds for a program whose funding authorization has expires. . . provides sufficient legal basis to continue the program during that period of availability, absent indication of contrary congressional intent.”<sup>5</sup>

Many crucial agencies and departments (over 256) are currently operating without authorizations, including the National Institutes of Health (NIH) (\$31 billion) and National Aeronautics and Space Administration (NASA) (\$19 billion). It is not as if the activities of these agencies are un-scrutinized by relevant authorizing committees or by appropriators. Only the defense authorization bill and, more recently, the intelligence authorization bill, are considered “must pass” bills and are enacted on a timely basis.

With today’s partisan polarization and obstructionism, it is hard to pass legislation, let alone consider the sheer number of expired authorizations that would have to pass to ensure all appropriations were authorized.

For example, the Foreign Relations Authorization Act has not been reauthorized

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<sup>4</sup> Congressional Research Service Report by Jessica Tollestrup and Brian T. Yeh, *Authorization of Appropriations: Procedural and Legal Issues*, September 9, 2014, p. 9.

<sup>5</sup> Government Accountability Office, Office of General Counsel, *Principles of Federal Appropriations Law*, Volume I, (3d ed. 2004) at 2-69. “It is fundamental . . . that one Congress cannot bind a future Congress and that Congress has full power to make an appropriation in excess of a cost limitation contained in the original authorization act. The authority is exercised as an incident to the power of the Congress to appropriate and regulate expenditures of the public money.”

for many years, at least partially because the politics over the mostly-unrelated issue of abortion. In this manner, partisan rancor, polarization and gridlock can (and frequently does) stop just about any reauthorization bill. An exception to the polarized gridlock last year was the reauthorization of The Every Student Succeeds Act programs that had received about \$22 billion in unauthorized appropriations in 2015 because of bipartisan leadership and compromise.

Just as in the earlier era of permanent authorizations, Congress picks and chooses which issues deserve floor time. The major difference now is that authorizations expire, but essential programs must be funded for essential services of government to function. However, controversies that should be resolved in authorization process spill over into appropriations and make it more difficult for the Congress to see that the government is funded for the coming year.

Even the most cursory review of the January 15, 2016 CBO's report on *Unauthorized Appropriations and Expiring Authorizations* demonstrates clearly why Congress has no choice but to fund programs it fails to authorize.

Should we shut down our air traffic control system and all commercial air travel in this country because the Senate Commerce Committee and the House Transportation and Infrastructure Committee cannot reach agreement on extending the FAA authorization?

Should investors be deprived of the regulatory protections provided them by Security and Exchange Commission because House and Senate Banking Committees do not send the President a new authorization?

Should citizens who live in the proximity of pipelines transporting hazardous

gases and fluids be deprived of federal monitoring of those lines until Congress reauthorizes that program?

Should our nation's veterans be deprived of needed medical care because large portions of the Department of Veterans Affairs have no current legislative authority other than that provided by appropriation law?

Obviously, government programs and activities are not unimportant because they have no authorization. The fact that the authorization process is broken is no reason to block the delivery of needed services and essential government activities.

While the decisions that the Congress must make with respect to funding government activities for which there is not authorization may be obvious, this Committee will perform a hugely important service to the Congress and to the nation if it can highlight as to why there are no updated authorizations for so much of the federal government. Unauthorized appropriations themselves are not themselves the problem. There are other basic problems with the current Congress that have caused the gridlock in passing authorizations.

I suggest political polarization and gridlock are the primary reasons so many programs are unauthorized.<sup>6</sup> Several solutions to polarization and the inability of Congress to pass authorizations in a timely fashion follow.

The extreme partisanship that seems to impact virtually every aspect of the

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<sup>6</sup> This problem is discussed more fully in James A. Thurber and Antoine Yoshinaka (Eds.), *American Gridlock: The Sources, Character, and Impact of Political Polarization* (Cambridge: Cambridge University Press, 2015).

legislative process and makes it more difficult to report legislation from committee, get the timely agreements needed in the Senate to bring legislation to the floor or reach compromise with the other body, and the White House to secure enactment. Authorizing committees deal with difficult policy issues and changes, which is their job. Absent the willingness of Members of Congress to cooperate and compromise, especially given their polarization on so many policy topics, it becomes difficult to pass stand-alone authorization measures. It takes special leadership, lots of time, and special circumstances to build the consensus to pass authorization bills such as the amendments to No Child Left Behind (The Every Student Succeeds Act of 2015) demonstrates.

The way Congress works or rather does not work, is aptly illustrated by the increasing number of unauthorized appropriations that are linked to polarization, and the unwillingness to compromise and work together. There may be an underlying desire for bipartisan lawmaking among Members of Congress of both parties (especially after they retire), but party leaders are structuring debates in recent years that promote, rather than deter, partisanship in some committees and on the floor. As a result, the chambers are more partisan and deadlocked than at any time since the 1860s (just prior to the Civil War). There is little consensus about major policy problems and authorizations of existing programs to solve some of those problems. It is harder than ever for a majority to foster the compromises that benefit the country, especially in the U.S. Senate. However, certain reforms would improve lawmaking and lead to more consistent and timely authorizations and careful oversight, encourage deliberation, and fulfill Congress's constitutional mandate to represent the people. Here are some suggestions:

Improve lawmaking through legislative procedural reforms. Return to the regular



order, limit restrictive rules, and improve protection of the minority. Congress also needs to return to real post-enactment conference committees that are transparent to the public and fair to both parties.

Of critical importance is requiring members of both chambers to spend more time on their jobs in Washington. The extraordinary amount of time now spent away from Washington, DC, and the work of Congress on fund raising by members in both bodies, undermines the capacity of Congress to make laws and do rigorous oversight. Former U.S. Senator Tom Daschle recently said that he thinks members of the Senate spend more time on fundraising than working in Congress. The Tuesday to Thursday Club needs to be stopped with an enforceable required schedule of work in Washington. Whether cutting the size of government or authorizing new programs, Members should be in Washington doing the work of committees, (oversight, deliberation, and lawmaking) as well as educating themselves in order to develop expertise to understand the substance of their assignment and how they can best set policy. It is time for the party leadership in both chambers to set rules of attendance that have consequences. The lack of time the Congress spends in session is directly related to the problem of unauthorized programs. There are roughly 280 days left before the November 8<sup>th</sup> election of which more than 200 are weekdays. But according to the schedule published recently by the House Majority Leader, the House of Representatives will be in session only 85 of those days and many of those are days in which members will need to appear in the House chamber for only a brief period at the end of the day for roll call votes or will vote well before noon before leaving for the airport and heading back to their districts. Even if those days are included in the count, the House will be completely out of session 60 percent of the weekdays

between now and the November election. The permanent campaign and the drive to solicit campaign money dominate the work of many members. There needs to be a new schedule for Congress in session, which includes not only the show time on the floor, but the work time in committees and their offices in Washington, DC, not their states and districts.

The inability of Congress – in the absence of a vigorous, hardworking, bipartisan center – to address effectively known problems and pass crucial authorizations in a timely way is a legitimate cause of public dissatisfaction. Trust in Congress is at historic lows for a reason.

The answer to a dysfunctional Congress is not to stop unauthorized appropriations. The answer is to get Congress to function. A Congress that cannot confront public policy challenges through timely authorizations will surely lack the reserves of comity and trust to face any unknown and sudden – and perhaps even more dangerous – crises.

Chairman ENZI. For all three of you, your entire testimony will be in there. We will also try and do hopefully a good job of summarizing it and getting that out to the Senators. And also the hearing stays open at the completion so that people can submit questions that we hope that you will also answer in a timely manner. People have until tomorrow night to get their additional questions in.

We will start the questioning then. I will start with Dr. Posner. Representative David Price testified before this Committee recently that the most careful and effective oversight Congress conducts is through the annual appropriations process. But I wonder if the annual appropriations process should be the sole arena for regular programmatic oversight. As a former Director of the Government Accountability Office, the legislative branch's watchdog agency that conducts audits and program review of Federal agencies, do you believe Congress is abandoning its oversight responsibilities in not reauthorizing its funds each year?

Mr. POSNER. Yes, I think you need more than one committee to be involved, and appropriators do a remarkable job with a huge set of issues. They have a certain orientation. They are operating against a fixed target.

They focus quite a bit on the line items and the specific personnel and positions and the like. I think authorizers are the program experts, and they have kind of the ability and the vantage point of focusing on the broader outcomes that we are expecting in these programs. They can look at evaluations and the like, and they do not have to do it every year for the most part, although some of them do it annually, as was said before.

So I think you need both perspectives to be applied in this process. If they conflict, I do not think that is unhealthy necessarily.

Chairman ENZI. Thank you. I mentioned in my opening statement that the Government Accountability Office has identified a frightening amount of program duplication across the executive branch, with multiple agencies essentially running parallel program operations like the STEM education program. I am concerned that instead of going back to review what we are spending money on, we are busy creating new programs. We get more credit for new programs and new money, and the new programs may be replicating activities done by the existing ones.

In each and every funded program, if each had to be reauthorized in order to receive appropriations, would we see less program duplication?

Mr. POSNER. Well, I think the best way to handle that is to start moving toward what I have called the "portfolio review," taking groups of related programs and looking at them together and bouncing them off against one another. We have 17 food safety programs. What is the relative cost effectiveness of the different ones? Are there economies of scale that we can use to move to a unified approach like we see in many other nations, for example? You know, we have programs in housing that are scattered across the tax and spending codes that sometimes work at cross-purposes.

For higher education, you cannot really understand the impact that higher education has on students, parents, and universities by looking at each program separately. You have to look at how they all work together or do not work together, and many of these sub-

sidies, for example, work at cross-purposes. You become eligible for one, you become ineligible for another.

And so I think only these more holistic reviews can really connect with the American people and their expectations for what Government should deliver. They do not have the time to, nor should they have to, parse out and unpack the byzantine program structure we have. We should be looking at the broader interface that Government has with them and have an oversight process that can get that done.

Chairman ENZI. Thank you. That reminded me that when we were doing those preschool programs, the big problem we ran into is that a bunch of them were not under our jurisdiction, which is why we could not eliminate duplication there. Our structure, as Dr. Thurber mentioned, is sometimes confusing and ineffective.

Ms. Tollestrup, in your testimony you describe the provisions in the Senate rules and House rules designed to curb unauthorized authorizations. These provisions have not been very useful in stemming the rising tide of unauthorized appropriations. We adopt hundreds of billions of dollars, as we have mentioned. Do you know how often these points of order have actually been invoked? And how could these points of order be given more teeth?

Ms. TOLLESTRUP. Senator, it is important to point out that Senate rules that prohibit unauthorized appropriations only apply to floor amendments, so only when those floor amendments are under consideration can such points of order be raised. The most recent instance that I am aware of was during the consideration of the fiscal year 2007 Department of Defense appropriations bill.

It is difficult to say what the length of time between this example and now means. It is possible that the rules are, in fact, deterring unauthorized appropriations from being offered as floor amendments, and so there were no other opportunities to raise points of order. It is also possible that there were opportunities, but those points of order were not, in fact, raised at that time.

In terms of options, CRS does not take a position on whether Rule XVI should be changed or what those changes should be. That is for Congress to decide. But if you were to look at amending Rule XVI so that it would potentially apply in more circumstances, having it apply to more than just individual amendments, such as committee amendments or bill text, or requiring that an authorization be enacted into law in order to for it to count for the purposes of the rule would both be possibilities.

Chairman ENZI. Thank you. My time has expired. I will come back with some more questions in a bit, and I will go to Senator Whitehouse.

Senator WHITEHOUSE. Thank you very much, Chairman. Let me stay with Ms. Tollestrup for a minute, and let me focus on the Senate, because I will start from the proposition that the rules in the House do not matter because whatever bill comes out, comes out with a rule that the Speaker's Rules Committee has put into play and that trumps everything else. But on the Senate side, we do not have that, the majority does not have that power. It is one of the blessings, I think, over here.

But as I understand your testimony, you are saying that if an expenditure is baked into an appropriations measure as it comes out

of the Appropriations Committee, there is no rule that would provide a point of order with respect to an unauthorized expenditure that is in that bill. It would have to be a floor amendment for there to be a procedure of any kind to challenge it.

Ms. TOLLESTRUP. That is correct. The prohibition on unauthorized appropriations only applies to individual floor amendments, so both the Appropriations Committee might offer a committee amendment containing an unauthorized appropriation, and unauthorized appropriations in the base bill text also are not subject to that prohibition.

Senator WHITEHOUSE. So if you are on an authorizing committee and the appropriators put funding towards a program either whose authorization has expired or they just invent it, there was never an authorization in the first place, as long as your first shot at it is on the Senate floor and as long as the Appropriations Committee got it into the measure that comes to the floor so it is not coming to the floor as an amendment, you are stuck, there is nothing that an authorizing committee person can do other than make noise, there is no rule?

Ms. TOLLESTRUP. So while there is no point of order that could be raised, that is correct, offering an amendment to take out the appropriation that is unauthorized would still remain an option.

Senator WHITEHOUSE. Yes, but then you would need 60 votes going your way, and it would not be there if they did not have 60 votes going their way. So good luck with that.

That is not a practical option from my view on the floor.

Dr. Posner, I was fascinated with your idea about changing the composition of this Committee a little bit. It may make sense to try to have the Finance Chair and Ranking and the Approps Chair and Ranking here so that they are a little bit more bought into this. I would hate to have it be all other folks because I think that Senator King's perspective—he is here—has been phenomenal. And as a former Governor, he has dealt with a lot of this and the fact that he is not senior enough to be in that little group, and I am sitting in what would be Senator Sanders' seat, and God knows he has got a perspective that has been noteworthy here in the Committee. So I would hate to see it turn into a pure leadership device, but leadership representation would be a very interesting idea.

I would also note that in other committees, bipartisanship can be a prerequisite for certain things, like a quorum, and because of that you cannot even get a subpoena out of a committee without bipartisanship. And yet we can get the entire budget of the United States out of this Committee without bipartisanship. So there is another angle that we could be looking at, that it is simply not in order for the Committee to produce a budget unless it has bipartisan support of some kind.

To your point about portfolios, we are not going to be able to jump in and do this without having tested the waters a little bit. It would be rash to do that and problematic. Is there an area that you would recommend to us as a particularly promising one for us to take a look at running the portfolio analysis that you described that would be small enough for us to actually bite it off and give it a whirl and that would potentially yield the opportunity for some significant reforms and consolidation of tax and spending policies?

Mr. POSNER. That is a good question. With the caveat there are no areas of low-hanging fruit in the budget, as you know, I think there are areas which lend themselves—higher education is one that I illustrated in my testimony, \$110 billion of Federal subsidy, 35 in the Tax Code, 70 through spending, through grants and loans and the guarantees and the like, as well as research and development.

I think one of the things that would be essential, of course, is forming a partnership with the authorizers. It makes some sense to think about the authorization schedules as they are, as thinking about how this might work as a prelude to the next authorization.

This Committee has actually taken some small steps in this direction. With Chairman Domenici, the Committee worked back in 2000 to create four task forces of the Senate Budget Committee to focus on broader policy areas. One was education that Senator Frist chaired. Another was foreign assistance. They took the entire 150 account, as they say downtown, the subfunction on international assistance, and did some broad oversight hearings on that function. I think Senator Sarbanes was involved with that. We had one on Social Security and one on another area. And several of them were productive of potential legislation, including the education one in particular.

So it is not a sure thing. It was the first time they tried this. It was during a time of surplus when, you know, the fiscal demands on the Committee were not as great and they could start to, you know, spread their wings.

I was hopeful that this might start getting the ball rolling, but it did not. But, nonetheless, there are ways that that could happen. I am struck when I look at legislatures—

Senator WHITEHOUSE. My time, Dr. Posner, has well expired, so let me—if you want to follow on with a written response for the record, I would be very interested in what your thoughts are.

Mr. POSNER. Sure.

Senator WHITEHOUSE. And that will give you a chance to deliberate even more. Thank you.

Chairman ENZI. Senator Perdue.

Senator PERDUE. Dr. Thurber, I have one word to describe my emotion in response to your testimony this morning, and that is, “Hallelujah.” I have been here just 1 year, but I have not heard anybody else come up here and talk about one of the fundamental problems of this body. And you have today, and I want to echo that.

Our Committee structure is just never going to work. It is not conducive with good stewardship of these issues. There are a lot of reasons why. I have gone back to 1946, looked at 1976, all the things in between in terms of how we got here. But when one Senator—and look at this Committee. I would argue that this topic right here addresses indirectly the number one crisis our country faces. It really does. These are all well-meaning men and women here on both sides of the aisle. And here we sit, because they are at another Committee at this very moment that they deemed was as important today. I have three myself at 10 o'clock, we all do, 10 o'clock this morning. This cannot continue. It does not work. It will never work.

The second thing, Dr. Posner, I know you have written several things, and I look forward to hopefully working with you and some of your organization about how to change this process. But I have a quick question, and that is, when you look at a budget—and I know Senator Kaine and Senator King and others have Governor experience, I come from business, where you look at the entire budget. And yet we spend \$3.7 trillion as a Federal Government, but we deal with \$1.1 trillion in this Committee. That is the first issue.

So the question I have is: How do you respond to my observation that, hey, wait a minute, why aren't we talking about all of it? My argument is heretofore when there were trust funds for Medicare and Social Security, I get it because they take care of themselves. Now they are not taking care of themselves, and we have line items on our budget that are supplementing both of those entities. So I would argue that gives us purview to bring all of the above spending into this Committee.

The second question that ties in with that—and I would love to hear your thoughts on this. First of all, the current process, I said with the other panel, it is set up for failure. Number one, it is a budget resolution. As Senator Whitehouse has said, the majority can cram down the throat of the minority any budget they want. And it is a political statement. We all know that. Even last year, this budget we produced was mostly a political statement. We crammed it down the throat of the minority. It did not get one vote. And then we go to authorization, and we find out, well, okay, some of those can get authorized, some cannot. But we get the appropriation, and now we really see the problem.

We can appropriate in the Committee, but the minority leadership has no incentive, Republican or Democrat, to ever let one of those appropriation bills get to the floor of the Senate. Why? Because the minority can drive an omnibus formula where they will get most of what they want. And guess what happens as a part of that process? We all spend more. Now, whether we think it is justified or not, that is the equation. It will never work. I have been sitting here for a year. I have been looking at for 3 years trying to figure out how well-intentioned and talented people end up spending money like we are spending, and now I get it. It is the process.

I applaud the Chairman and the Ranking Member, and I know Senator Whitehouse and Senator King have spoken out on this, among others. But I would love to get your thoughts about what keeps us from bringing all that in. And then is it not time that we throw the 1974 act out and take a start at this from a clean page perspective? I would like to get you and Dr. Thurber on that as well.

Mr. POSNER. I think it is an important question because we now focus on 30 percent of the total.

Senator PERDUE. Exactly.

Mr. POSNER. And we need to have regular ways to bring them all together, which is why I suggested this portfolio approach. You would bring the whole thing together regardless of the character.

Senator PERDUE. That would include mandatory—

Mr. POSNER. Exactly. Mandatory and discretionary and tax expenditures. Part of this process is that this Committee legislates the whole, sometimes there is tension with the specific committees. For instance, it is very tempting to articulate symbolic 302(a)s that are completely incapable of ever being implemented. And I think that is why having a leadership presence on this Committee might help temper that process. Bringing more players into the process of formulating the whole might help the budget be more realistic and more grounded.

In our National Budget Roundtable, we have some questions that we are starting to look at about how you budget for entitlements. Can we bring them into play more regularly? You do not put a cap and do them every year, but can there be meaningful targets that are adjusted every 5 years with some points of order around it?

Senator PERDUE. Dr. Thurber.

Mr. THURBER. A couple of comments. One, on an earlier comment that you made about the committee system, I want to remind you that there are 109 committees and subcommittees dealing with homeland security; there are 58 dealing with energy and environment. One of the toughest things that you can do is to realign jurisdictions. It is like playing Monopoly, and the Chair of Appropriations and Finance have Boardwalk and Park Place. No one wants to give up jurisdiction. Jurisdiction is power and power is a very difficult thing to give up. Committee reform needs to be done on a regular basis because of program duplication. Multiple overlapping jurisdictions is a major source of conflict and dysfunction on the Hill. And it is not the executive branch's fault. It is the growth in the number of committees and subcommittees.

Senator PERDUE. But therein lies the dysfunction in the Federal Government, in my mind. I understand the balance of powers between the branches, but we see the rise of the regulatory side right now that does not have that encumbrance. They are much more productive in producing rules that have a dramatic impact on our lives, whereas we get stumped here trying to fight through this maze to get any change. I am sorry to interrupt, but—

Mr. THURBER. Congressional gridlock shifts power to the executive branch.

Senator PERDUE. That is what we have done. That is what Senator Whitehouse said, and I agree.

Mr. THURBER. Putting leadership, Ways and Means and Appropriations, on this Committee, as they do in the House is a good idea. It is a good idea to have that representation on this Committee to help bring senators together before you go forward with a concurrent budget resolution.

Senator PERDUE. Thank you.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Senator KING.

Senator KING. Thank you, Mr. Chairman. I want to thank you for calling this hearing because I think we have really had some provocative and important testimony.

Dr. Thurber, before we get into the substance of budget, I was fascinated by your research about partisanship and partisan divide going back to 1860. I would like to request that you, as much as



possible, correlate that to the esteem in which the institution is held. It would be very interesting to line those up. I suspect you would see that there is a direct correlation between partisanship and low esteem.

Mr. THURBER. If I might answer immediately?

Senator KING. Sure.

Mr. THURBER. I do not want to push my book that just came out, "American Gridlock," but in it we show a relationship there between support as measured by Gallup and others and the amount of polarization. I blame the polarization on both parties. There is nobody in the middle anymore.

Senator KING. If you did not push your book, you would be the first witness in a congressional committee not to do so. I welcome that.

The issue, it is not 30 percent, David. It is more like 20 percent, because tax expenditures are part of this, too. My numbers are 1.1 on discretionary, about 2.6 on mandatory, 1.4 on tax expenditures. Tax expenditures are the granddaddy of all unauthorized programs. They are authorized once. The efficacy is never tested. The need is never tested. The relevance is never tested. And they are there forever, and we extended a bunch of them forever just this past December without regard to its impact on the long-term budget. The tax expenditures now exceed the actual tax revenues. So if we are going to talk about this, Mr. Chairman, I think we need to talk about the whole budget, I think it is \$5.1 trillion. My mother used to have a wonderful saying. She said, "You are straining at gnats and swallowing camels." And by focusing all our attention on the funding for Head Start or whether or not to buy an aircraft carrier, we are missing a much, much larger picture.

Mr. Posner, I thought your idea about reviewing programs as a group is very insightful and important. But the question is—and it gets back to the discussion we have been having—who does it? Is it this Committee? Is it the authorizing committees? Is it the Appropriations Committee?

Maybe we ought to have a new committee called "Oversight" whose sole responsibility it is to do that. It would not be a very glamorous one. But your thoughts on—you know, I think your insight is accurate, but who does it?

Mr. POSNER. That is, obviously, the big question. I think this Committee could do it. This is why I suggested this be anchored as a leadership committee because then it would be easier to orchestrate. I think it also could become a joint committee in its initiative, possibly, and it would have to be something the leadership would have to bless, and it would have to be something that would be a high priority even with the President to support it.

So I think there are several different avenues for that, but this Committee was intended to take a look at the broad missions of Government through the budget function, 19 of them. And there are 96 subfunctions, and they cut across all the programs, not including tax expenditures. That is the way the resolution was supposed to be allocated, and those figures are nice and analytic, tidy little sums in the resolution, but they are never used you the Congress to budget or manage or oversee.

What I am saying is let us give life to those concepts because they are sorely needed as Government has grown and become more fragmented. And, obviously, the question is raised: Which committee does that? And I think it probably has to be several working together in some way. But, I think this Committee needs to lead it.

Senator KING. Mr. Thurber, do you have thoughts on that?

Mr. THURBER. Yes. Under the rules of the House and the Senate, when committees go forward to get funding, they are supposed to produce an oversight calendar, and that should be one of the criteria for funding committees. Leadership could be involved to make sure that committees are working together in their oversight on that calendar. It is very hard to enforce. It really is not being enforced. One possibility is to have two or more committees coordinate their oversight calendars. They could plan Joint Oversight to improve deliberation and lawmaking. And if they cooperated, they could get an appropriation for their committee.

Senator KING. I think you made a very important point, and I have talked about this at home in Maine about how to overcome this partisanship. A lot of it comes down to people. It is no coincidence that Lamar Alexander and Patty Murray were the Chair and Ranking Member of that Education Committee that got the major education bill through. I believe that a lot of it is the individuals that are in the seats and whether they are inclined to try to work things out. The Chairman of this Committee has had that same kind of experience.

Mr. THURBER. I agree with that. I hate to go back to ancient history when budget chair Muskie and ranking member Bellmon got along very well, but it is a good example. They were former Governors, by the way, that knew how to put budgets together, which helped in bipartisan collaboration. Their cooperation and their personalities really launched the Budget Impoundment Control Act of 1974. The budget process was successful during their tenure as a result of their leadership.

Senator KING. I think you and I may have served together. I was on the staff here from 1973 to 1975.

Mr. THURBER. Yes.

Senator King. It is quite an experience to come back 40 years later as a Senator, having seen the differences.

Again, Mr. Chairman, thank you. I think this is so important, and we have got to continue to talk about this. And we also have to continue to talk about why is it, even in good times—we are in relatively good times now. Why is it that we cannot balance the budget? But we cannot balance it entirely on that 22 percent of the budget.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

You pushed your button. Did you want to make another—

Senator WHITEHOUSE. No. I was just going to blame Senator King for how bad things have turned since 1975 when he left. [Laughter.]

Everything just went straight downhill. But luckily he is back now to help straighten this out.

Senator PERDUE. Mr. Chairman.

Chairman ENZI. Senator Perdue.

Senator PERDUE. Would you indulge me with one last question before we—

Chairman ENZI. Sure.

Senator PERDUE. I apologize. I would love to get all your responses to no matter what the process is, there are the dates and accountability, but there is no accountability here. If we do not do a budget by April 15th, if we do not fund the Government and pass all the appropriations by September 30th, there are too many easy release valves. You can do a CR. You can do an omnibus, minibuss, all these combinations. Only four times in the last 4 years have we really operated this thing responsibly. So I know the process is wrong. But even within that, there is no consequence for non-performance.

Have you guys looked at—and there are best practices around. I mean, States do this all the time. Many States have a balanced budget law. They have control of this. They get their budgets done. And, by the way, most of them do it in 45 days or less. My question is: Have any of you looked at the types of consequences that other entities like this use to enforce performance?

Mr. POSNER. I can start that off. The States have something that we do not. They have aggressive bond markets that vigilantly oversee them. The constitutional requirements aside for balanced budgets, they have aggressive bond markets.

Senator PERDUE. We have the Federal Reserve.

Mr. POSNER. Well, we have generous bond markets at this point. So from that standpoint—and the States do, in fairness, as we see in Illinois now and other States, extend deadlines when they cannot reach agreement as well. But I think the overall constraints bearing on States or other countries which I have studied are far more impressive to policymakers than they are to our policymakers at this point.

Senator PERDUE. Well, some of those States—Illinois is not one of them—actually have a balanced budget law.

Mr. POSNER. Yeah.

Senator PERDUE. So that really is sort of an end consequence that you—it is a law, and you have got to adhere to it.

Mr. POSNER. Yeah, yeah, enforced by the bond markets. Right.

Mr. THURBER. Let me say that since the 1974 budget act was passed and fully implemented in 1976, we have changed the budget process every few years. So you have asked, Are there mechanisms to force people to make decisions? Well, we tried with the original act, with Gramm-Rudman-Hollings I and Gramm-Rudman-Hollings II, and then we tried with the 2011 act where if you did not act in time (the super committee did not deliver in a certain amount of time) budgeting and appropriations became an automatic “meat-axe” approach through sequestration.

If you do not change the will of the members to cooperate—your reforms will not have a major impact. That means you have to go back to the way people are elected. The polarization of the American voters, the polarization of the media, the polarization of interest groups, the polarization of State legislatures as well as this body undermine bipartisanship and cooperation, necessary for the congress to function. I do not see any immediate magical ways to

change that polarization and gridlock. If you cannot do that, then instituting a new Budget and Appropriation process may not work.

Senator PERDUE. You may have just gotten outside the scope of this Committee just a bit.

Mr. THURBER. I did.

Chairman ENZI. Nothing is outside the scope of this Committee. [Laughter.]

Mr. THURBER. I apologize for that, Senator.

Senator PERDUE. No, no. You are fine.

Ms. TOLLESTRUP. So while I am not able to speak today to balanced budget and those kinds of requirements that exist in different entities, I can talk a little bit about what mechanisms Congress does have to encourage timely legislative review when it comes to how the laws are put together.

The focus of this hearing has been expired authorizations of appropriations, and those provisions expiring can provide an occasion for legislative review and for new laws to be enacted. But if those provisions expire, they do not themselves terminate the program. They simply terminate the authorization of appropriations.

There are other kinds of provisions in laws that can expire and also provide occasion for legislative review. For instance, mandatory or revenue-related provisions, authorities for user fees, those are the sorts of things that encourage legislative review when it comes to laws like surface transportation, the farm bill, programs like that.

Essential authorities also can expire, including authorities that relate to how a program will function. For instance, certain investigative authorities under the PATRIOT Act expire on a certain calendar, and that encourages legislative review on that schedule.

And then also Congress does have the option of sunseting a program and having a sunset built into the law. So as is the case with the Export-Import Bank, with terrorism risk insurance, there are different ways that Congress has approached trying to sunset programs on a schedule in the past.

Senator PERDUE. Yes, I am less concerned about the programs. I know that was a focus, and that is a great answer. I really am asking the question that, you know, if we cannot fund the budget by the deadline, I mean, what consequences are there? And we found too many release valves that give us a way out of the box, and the release valve is more spending. And that is the reality that we have got.

Mr. Chairman, I am sorry. I have overstayed my time. Thank you.

Chairman ENZI. Well, I want to thank the witnesses. I have got to go back through pages and pages of notes that I have made as a result of what you have suggested. I think there are a lot of good suggestions there, and I have asked Senator Whitehouse to share with me any inspirations that he has.

The one comment that I made was that we require the President to give us his budget by a specific time. In my 20 years here, the only use that I have seen for that is for one party to beat up on the President's budget and the other party to proclaim the intelligence of that budget. And the budget format is not even in the same format that we use, so what he gives us is not usable. I am

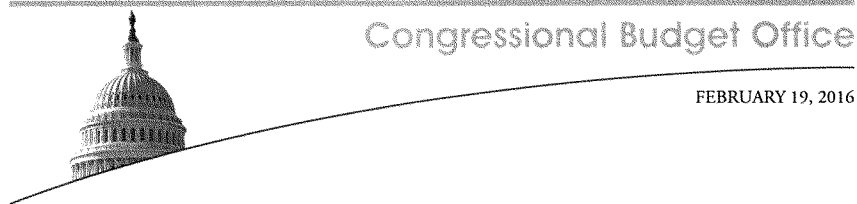
hoping that it is usable from a management standpoint, from an administrative standpoint, but somehow the two of us, the two bodies, need to get together on making that more effective one way or another.

The oversight process I think creates some problems because it usually results in taking money away, and we are much more excited about giving money away than stealing money. The consequences are considerably different.

So thanks for all of your suggestions and for your outstanding testimony, and we will be trying to—we will be getting some more information out to members of the Committee that were not here.

Thank you. Excellent panel. The hearing is adjourned.

[Whereupon, at 11:47 a.m., the Committee was adjourned.]



**Answers to Questions for the Record  
Following a Hearing on Unauthorized Appropriations  
Conducted by the Senate Budget Committee**

*On February 3, 2016, the Senate Budget Committee convened a hearing at which Keith Hall, Director of the Congressional Budget Office, testified about appropriations with expired authorizations. After the hearing, Chairman Enzi and Senator Perdue submitted questions for the record. This document provides CBO's answers.*

**Chairman Enzi**

**Question.** We know that some programs whose authorization is current do not have specific authorization levels; they are authorized to receive "such sums" as the appropriators deem appropriate. But by authorizing no specific level of funding, no budgetary guidepost is created for funding decisions. Should we do away with "such sums" authorization levels? Is a "such sums" authorization level more useful than having no authorization at all?

**Answer.** A "such sums" authorization provides no guidance about the amount of funding that may be appropriate, but if it specifies a certain number of years, it at least sets a time horizon for the authorization. An authorizing committee can use a "such sums" authorization to formally indicate that it does not have a strong basis for providing specific guidance to the appropriations committee about the funding needed for programs for a particular period of time. It may prefer to focus its efforts during the authorization process on addressing policy issues that it directly controls rather than on advising the appropriations committees on dollar amounts. But if a "such sums" authorization has no time horizon, then when the committee would be expected to revisit the substance of the program or its funding in the future is unclear. (CBO does not make recommendations about what the Congress should do.)

**Question.** Some of the programs in CBO's report have been unauthorized for decades. It is one thing for a program's authorization to expire before it can be renewed, but these programs are persistently unauthorized for long periods of time. Congress has for one reason or another not come to consensus on renewing their charter, and yet never fails to provide them annual funding. Does it make sense to have a period of time after which the ability to fund an expired program without authorization sunsets?

**Answer.** There is certainly value in reassessing spending programs—both mandatory and discretionary—and tax provisions on a regular basis as circumstances change and as more information becomes available about how those programs or provisions are functioning. If, after a certain period of time beyond the expiration of an explicit authorization of appropriation, a discretionary program could no longer be funded through appropriations, more attention would probably be paid to such authorizations. (Again, CBO does not make recommendations about what the Congress should do.)

**Question.** Senator Rand Paul (R-KY) recently introduced the Legislative Performance Review Act, S. 2454. Among other provisions, this bill would “wind down” programs over two years once their authorization expires. And it would create a surgical point of order—with a 3/5 vote necessary to waive—against a provision in an appropriations bill funding a program for a fiscal year in which it is not specifically authorized. What do you expect the practical impact of S. 2454 would be, if it were to become law?

**Answer.** With such a point of order available to Members, more attention would probably be paid to ensuring that programs, particularly those that might be controversial, had current authorizations of appropriations.

**Question.** One authorization that never fails to occur on an annual basis is the defense authorization bill. That is why our discussion today is focused on non-defense discretionary spending. What is it about the defense authorization bill that enables it to clear Congress each year, when so many other authorization laws expire before they can be addressed?

**Answer.** CBO has not attempted to analyze differences between Congressional processes used to determine defense and nondefense discretionary funding. One analyst from the Congressional Research Service who has studied that question argues that “a complex mixture of committee traditions, rules, processes, a robust hearing schedule, bipartisanship, professional staff relationships, floor strategy, and a widely shared belief in the overall mission contribute to the outcome.”<sup>1</sup>

#### Senator Perdue

**Question.** Since 2011, the GAO has produced a yearly report on “Opportunities to Reduce Fragmentation, Overlap, and Duplication.” Over the past five annual reports, GAO has recommended approximately 440 actions that Congress and the executive branch could take to improve fragmentation, overlap, and duplication within the Federal government to help achieve financial benefits. Could your office work with the GAO to assess how many of these actions were related to programming whose authorization lapsed?

**Answer.** Yes, CBO will consult with the staff of the Government Accountability Office and assess the feasibility of determining which explicit authorizations of appropriations that have expired were also identified in GAO’s analyses of fragmentation, overlap, and duplication. Cross-walking the information in CBO’s report *Unauthorized Appropriations and Expiring Authorizations* with the information in GAO’s report on fragmentation, duplication, and overlap is likely to be quite challenging, but if we are able to find programs identified in both reports, we will work with the staff of the budget committee to determine the best way to make that information available.

1. See Colleen Shogan, “Defense Authorization,” in Jacob Straus, ed., *Party and Procedure in the United States Congress*, (Rowman & Littlefield, 2012), pp. 195–216, <https://rowman.com/ISBN/9781442211735/Party-and-Procedure-in-the-United-States-Congress>.



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**MEMORANDUM**

February 24, 2016

**To:** Senate Budget Committee  
Attention: Peter Warren

**From:** Jessica Tollestrup, Specialist on Congress and the Legislative Process,  
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**Subject:** Questions for the Record (February 3, 2016)

This memorandum responds to the questions you submitted for the record of a hearing held by the Senate Budget Committee on February 3, 2016, at which Jessica Tollestrup testified on behalf of the Congressional Research Service (CRS). The hearing examined budget process issues associated with unauthorized appropriations.

The listed authors have prepared the following responses to the questions you submitted to CRS. Each question and response is presented separately below in the same order as outlined in the letter from Chairman Enzi that was sent to Jessica Tollestrup on February 3, 2016.

**1. We know that some programs whose authorization is current do not have specific authorization levels; they are authorized to receive “such sums” as the appropriators deem appropriate. But by authorizing no specific level of funding, no budgetary guidepost is created for funding decisions.**

**a. Should we do away with “such sums” authorization levels?**

**b. Is a “such sums” authorization level more useful than having no authorization at all?**

CRS takes no position on whether certain forms of authorizations of appropriations are preferable to others. Historically, as well as in current practice, there have been no congressional rules that stipulate a certain form for authorization laws, or require that appropriations for government agencies, programs, and activities be explicitly authorized. As a consequence, the authorizing committees (and Congress more generally) have a range of options available to them—from providing no explicit authorization of appropriations, to providing an explicit authorization that is definite in terms of amount and/or time.<sup>1</sup>

As was outlined in the written testimony previously submitted for the record, the purpose and form of authorizations has changed in a number of important ways over the past century. Prior to the mid-twentieth century, authorizations tended to provide broad grants of authority on a permanent basis, with

<sup>1</sup> This response is largely drawn from CRS Report R43862, *Changes in the Purposes and Frequency of Authorizations of Appropriations*, by Jessica Tollestrup.



no explicit references to amounts that would be appropriated in the future. Such authorizations provided a sufficient basis for those authorized purposes to subsequently be funded through the annual appropriations process. When the authorizing committees began to include explicit authorizations of appropriations in certain circumstances, these represented an assertion of the role of those laws—and, indirectly, role of the authorizing committees themselves—in budgetary decisionmaking. The authorizing committee might have made a determination as to whether such an assertion was warranted in a particular circumstance based on a variety of factors such as the funding and oversight needs of the relevant agency, activity, or program, as well as the extent to which budgetary decisionmaking through the appropriations process was producing outcomes that were satisfactory from an authorization perspective.

In choosing to include an explicit authorization of appropriations, authorizing committees further needed to decide whether such an authorization should be limited as to time or amount. The time period could be permanent or specified. Likewise, the amount could be indefinite (e.g., “such sums as are necessary”) or definite (i.e., \$10 million). Choosing a specific time period or definite amount (or both) would require further legislative action whenever those authorizations of appropriations expired (or the amounts otherwise needed to be altered) in order to satisfy requirements under congressional rules that appropriations be authorized. Whichever combination of options was chosen in a particular context would reflect whether legislatively addressing the entity’s funding needs (and also possibly their programmatic needs) on a regular basis was expected to be beneficial from an oversight or funding perspective. On the one hand, the committee might determine that such an expectation of regular legislative action would enhance their oversight of that entity, or that the opportunity to regularly weigh in as to funding levels would give the committee a procedural tool to influence budgetary decisionmaking. On the other hand, the committee might decide that it would be better to address the entity legislatively on an as-needed basis. It also might prefer to leave the amount of the authorization of appropriations unspecified to preserve flexibility for the appropriations process so that decisions about the amount to be appropriated could be made in light of current budgetary constraints. In other words, the committee might decide that it was enough to assert the role of authorizations in appropriations decisionmaking, but that no further funding direction or expectation as to periodic legislative action was warranted.

Whatever determinations are made by the authorizing committees (and Congress as a whole) that are based on the considerations outlined above may lead to different authorization outcomes in different contexts.

**2. Some of the programs in CBO’s report have been unauthorized for decades. It is one thing for a program’s authorization to expire before it can be renewed, but these programs are persistently unauthorized for long periods of time. Congress has for one reason or another not come to a consensus on renewing their charter, and yet never fails to provide them annual funding. Does it make sense to have a period of time after which the ability to fund an expired program without authorization sunsets?**

CRS takes no position on whether it would be legally or procedurally advisable to prohibit appropriations when the relevant authorization of appropriations has expired. However, if Congress wanted to prohibit unauthorized appropriations more broadly than what is provided under current law, or in House and Senate Rules, the ability to override any new legal requirements, or waive those new rules, would continue to be in effect.

There are existing statutory requirements that a specific authorization must be enacted before appropriations may be expended by certain agencies or for certain activities. For example, 10 U.S.C. § 114 requires funds appropriated for various defense-related activities to be preceded by a law specifically authorizing funds for those purposes. However, GAO has taken the view that such a provision is merely a

directive from Congress to itself, and that if Congress goes on to appropriate funds in violation of 10 U.S.C. § 114, “there are no practical consequences.”<sup>2</sup>

In addition, certain governmental entities and activities are structured to sunset after a certain time period, after which the legal authority for that entity or activity ceases to exist. For example, the Export Import Bank is currently subject to a sunset date of September 30, 2019.<sup>3</sup> As with lapses in authorizations of appropriations, an appropriation of funds to an entity whose substantive authority has lapsed may be viewed as an extension of that substantive authority for the period of availability of the funds.<sup>4</sup>

Besides the ability to override statutory requirements for explicit authorization and provide implicit extensions of authority through the appropriations process, the existing congressional rules that prohibit unauthorized appropriations may be waived through a number of mechanisms. House Rule XXI(2)(a) prohibits unauthorized appropriations in both the text of a general appropriations measure and any amendments thereto.<sup>5</sup> That House rule may be waived by three different mechanisms—a special rule that is adopted by a majority of Members voting and includes a waiver of Rule XXI(2)(a),<sup>6</sup> a motion to suspend the rules that is adopted by two-thirds of Members voting,<sup>7</sup> or by unanimous consent. Senate Rule XVI(1) prohibits appropriations not authorized by law in amendments offered by individual Senators.<sup>8</sup> That Senate rule may be waived by two different mechanisms—a motion to suspend Rule XVI(1) that is adopted by two-thirds of Senators,<sup>9</sup> or unanimous consent.

Even if the House and Senate chose to alter the waiver mechanisms that are currently available to them, they would continue to maintain their constitutional authority in Article 1, Section 5, to determine the rules of their own proceedings. This would always include the possibility of overriding any rule in any particular case, including those that prohibit unauthorized appropriations.

**3) Senator Rand Paul (R-KY) recently introduced the Legislative Performance Review Act, S. 2454. Among other provisions, this bill would “wind down” programs over two years once their authorization expires. And it would create a surgical point of order—with a 3/5<sup>th</sup> vote necessary to waive—against a provision in an appropriations bill funding a program for a fiscal year in which it is not specifically authorized. What do you expect the practical impact of S. 2454 would be, if it were to become law?**

<sup>2</sup> GAO, 1 Principles of Federal Appropriations Law 2-42 (Jan. 2004).

<sup>3</sup> 12 U.S.C. § 635f, as amended by P.L. 114-94, § 54001(a).

<sup>4</sup> 71 Comp. Gen. 378 (1992) (finding that an appropriation specifically for the U.S. Civil Rights Commission for part of FY1992 overrode a prior law that would have sunset the Commission at the end of FY1991).

<sup>5</sup> For further information with regard to the operation of House Rule XXI(2)(a), see CRS Report R42098, *Authorization of Appropriations: Procedural and Legal Issues*, by Jessica Tollestrup and Brian T. Yeh, pp. 4-6.

<sup>6</sup> A special rule is a House resolution that is intended to regulate floor consideration of a specific measure or matter, including by superseding the standing rules of the House. For general information about special rules and the waiver of House rules, see CRS Report 98-433, *Special Rules and Waivers of House Rules*, by Megan S. Lynch. For information on the historical frequency of such waivers for the initial consideration of regular appropriations measures, see CRS Report R42933, *Regular Appropriations Bills: Terms of Initial Consideration and Amendment in the House, FY1996-FY2015*, by Jessica Tollestrup, Table 4.

<sup>7</sup> House Rule XV(1) provides for procedures to suspend the rules of the House. For further information about the suspension procedure, see CRS Report 98-314, *Suspension of the Rules in the House: Principal Features*, by Elizabeth Rybicki.

<sup>8</sup> For further information with regard to the operation of House Rule XXI(2)(a), see CRS Report R42098, *Authorization of Appropriations: Procedural and Legal Issues*, by Jessica Tollestrup and Brian T. Yeh, pp. 6-8.

<sup>9</sup> Motions to suspend the rules of the Senate are governed by Rule V, XII, XIX, and numerous precedents. For further information with regard to procedures to consider motions to suspend the rules in the Senate, see *Riddick's Senate Procedure*, pp. 1266-1272.

S. 2654 would seek to make a number of changes to the budget process related to the purpose and frequency of authorizations of appropriations. These changes appear to be premised on an expectation that authorizations of appropriations should be explicit, time limited, and for definite dollar amounts. In addition, it appears that such authorizations of appropriations are expected to be at a level specific to one or more individual “programs.” The legislation defines “program” to mean “any activities or purposes for which there is a separate authorization of new budget authority” (Sec. 2(5)). The proposal does not reference authorizations of appropriations for other purposes (i.e., departments, agencies). Currently, there are no congressional rules that require authorization laws to take a certain form, and the form of those laws has wide variation in current practice. In addition, there is no universal definition or understanding of what constitutes a program for the purpose of day-to-day management or the federal budget process.<sup>10</sup> As a consequence, the “practical impacts” of this proposal if it were to be adopted would depend on how it is understood and applied by Congress and the executive branch in a particular context. CRS is unable to generalize as to what those impacts might be.

The mechanism referenced in your question that relates to the “wind down” of programs is in Section 8 of S. 2654. Section 8 is generally triggered when the authorization of appropriations for a program has lapsed. In such an event, the head of the agency carrying out the program is directed to terminate the activities conducted under the program; transfer, or otherwise dispose of, the records, property, and personnel affected by the termination of the program; and transfer unexpended balances of appropriations and other funds.

Section 8 also provides a mechanism by which the termination of a program for which the authorization of appropriations has lapsed can be delayed. Specifically, if either the House or Senate passes a bill which is not enacted into law, but would have extended the authorization of appropriations or provided a new authorization of appropriations for the program, new budget authority for the program will continue to be authorized for an additional two fiscal years, albeit at a reduced rate. The authorization of appropriations for the first year will be 80% of the amount appropriated for the program in the last year of the lapsed authorization of appropriations, and 60% of the same amount for the second fiscal year following the lapse. If Congress subsequently reauthorizes appropriations for the program, then that level of authorization will replace the tapered levels described above. This tapered level is also not available if Congress affirmatively repeals an authorization of appropriations, instead of simply letting an authorization reach its sunset date.

Although GAO has recently opined that “[w]e do not read the absence of an authorization of appropriations to defeat clearly established program authorities set out in the enabling legislation,”<sup>11</sup> the enactment of Section 8 may be viewed as modifying the enabling legislation of a program whose

<sup>10</sup> As discussed in a CRS report, “depending on an observer’s preference, the term may include any government function, policy, activity, project, initiative, law, tax provision, or group thereof.” See the “Glossary of Terms” in CRS Report R42379, *Changes to the Government Performance and Results Act (GPRA): Overview of the New Framework of Products and Processes*, by Clinton T. Brass. For example, the term program may have different meanings in different contexts, and different meanings across several participants or observers within the same context, including for purposes of appropriations, authorizing acts, federal grant-making authorities, government organization, and management of government activities within and across agencies. Relatedly, the U.S. Federal Accounting Standards Advisory Board (FASAB) has stated that “there is no firm definition for the term ‘program;’ it varies in the eye of the beholder.” U.S. Federal Accounting Standards Advisory Board, *Statement of Federal Financial Accounting Concepts 2, Entity and Display*, June 6, 1995, at [http://files.fasab.gov/pdffiles/handbook\\_sffac\\_2.pdf](http://files.fasab.gov/pdffiles/handbook_sffac_2.pdf).

<sup>11</sup> GAO, *Social Security Administration—Work Incentives Planning and Assistance Program (WIPA) and Protection and Advocacy for Beneficiaries of Social Security Program (PABSS)*, B-323433 (Aug. 14, 2012). See also Office of Legal Counsel, *Availability of Appropriations for Social Security Administration Grant Programs Following the Expiration of Authorizations of Appropriations*, 2013 WL 11105737 (Feb. 4, 2013) (“When an agency has legal authority to administer a program and appropriated funds are available for that purpose, the absence or expiration of an authorization of appropriations does not prevent the agency from expending funds on the program unless such a restriction is imposed by statute.”).

authorization of appropriations has terminated, specifically by requiring the “terminat[ion] of the activities under the program.”<sup>12</sup>

Additionally, the delay mechanism may be legally suspect because it purports to suspend an agency head’s termination obligations under the law based solely upon the actions of a single chamber of Congress. Such a mechanism would not appear to satisfy the constitutional requirements of bicameralism and presentment,<sup>13</sup> and the Supreme Court has previously found a similar procedure to be unconstitutional in the context of a one-House legislative veto.<sup>14</sup> If the delay mechanism is found to be unconstitutional, then a court will have to determine whether it is severable from the rest of Section 8. If the unconstitutional provision can be severed, then the program termination directed by Section 8 could only be avoided if Congress affirmatively extended the authorization of appropriations for a program or otherwise waived the applicability of Section 8, through a law passed by both chambers and signed by the President or enacted over a Presidential veto. It is possible that such a waiver could occur through a law appropriating funds to the program beyond the sunset of its authorization of appropriations, if Congress makes clear its intent to allow the program to continue operating.<sup>15</sup>

In addition, your question references a new point of order against unauthorized appropriations that would be created by Section 10 of S. 2654. Section 10(a) provides that it will not be in order in the House or Senate to consider a measure containing appropriations for a program that are “not made pursuant to a law in effect authorizing new budget authority for the program.” Section 10(b) further provides that such points of order in the Senate be raised as provided in Section 313(e) of the Congressional Budget Act of 1974, and allows that such a point of order may be waived upon an affirmative vote of three-fifths Members (duly chosen and sworn) in accordance with the procedures in that section of the Budget Act.<sup>16</sup> Further, Section 10(c) provides specific procedures in the Senate to dispose of a conference report or amendment between the houses that has had a point of order sustained against it under subsection (b). This proposal does not provide a specific mechanism for the House consideration of points of order under Section 10.<sup>17</sup>

The procedural approach to unauthorized appropriations that is taken by Section 10 is to create a point of order that would be in addition to the existing points of order in House Rule XXI(2)(a) and Senate Rule XVI (1). (These existing points of order are discussed in the written testimony previously submitted for the record.<sup>18</sup>) Unlike the existing House and Senate Rules, however, the Section 10 point of order appears

<sup>12</sup> S. 2454, § 8(d)(3).

<sup>13</sup> U.S. Const. Art. I, § 7, cl. 2 (“Every Bill which shall have passed the House of Representatives and the Senate, shall, before it become a Law, be presented to the President of the United States; If he approves he shall sign it, but if not he shall return it, with his Objections to that House in which it shall have originated, who shall enter the Objections at large on their Journal, and proceed to reconsider it. If after such Reconsideration two thirds of that House shall agree to pass the Bill, it shall be sent, together with the Objections, to the other House, by which it shall likewise be reconsidered, and if approved by two thirds of that House, it shall become a Law.”).

<sup>14</sup> *INS v. Chadha*, 462 U.S. 919 (1983).

<sup>15</sup> See *U.S. v. Will*, 449 U.S. 200, 221-24 (1995), and 71 Comp. Gen. 378 (1992) (finding that an appropriation specifically for the U.S. Civil Rights Commission for part of FY1992 overrode a prior law that would have sunset the Commission at the end of FY1991).

<sup>16</sup> Section 313 of the Congressional Budget Act, sometimes referred to as the “Byrd Rule,” allows a point of order to be raised against “extraneous matter” during the consideration of reconciliation measures. For further information, see CRS Report RL30862, *The Budget Reconciliation Process: The Senate’s “Byrd Rule”*, by Bill Heniff Jr.

<sup>17</sup> Presumably, such points of order could be addressed through the regular procedures of the House (including those that provide for the suspension of the rules) or by provisions in a special rule. For further information, see CRS Report 98-307, *Points of Order, Rulings, and Appeals in the House of Representatives*, by Valerie Heitshusen and CRS Report 98-433, *Special Rules and Waivers of House Rules*, by Megan S. Lynch.

<sup>18</sup> For further information, see also CRS Report R42098, *Authorization of Appropriations: Procedural and Legal Issues*, by Jessica Tollestrup and Brian T. Yeh.

to be intended to apply only to provisions in appropriations measures, and not amendments thereto. An additional point of difference is the criteria that an appropriation must meet in order to be authorized. Section 10 appears to expect that authorizations of appropriations take a particular form with regard to specific programs or purposes, and not be provided at a broad or implicit level as is allowed by House Rule XXI and Senate Rule XVI. Were both the existing chamber rules and Section 10 to operate simultaneously, these differences in application and criteria might present two sets of challenges. First, the Appropriations Committees might find it difficult to determine which of the criteria for authorization of appropriations should apply in a particular circumstance. Second, the fact that the rules would apply in different, and sometimes overlapping, procedural circumstances could make it difficult for the House or the Senate to consistently and predictably address unauthorized appropriations during the floor consideration of appropriations measures.

**4) One authorization that never fails to occur on an annual basis is the defense authorization bill. That is why our discussion today is focused on non-defense discretionary spending. What is it about the defense authorization bill that enables it to clear Congress each year, when so many other authorization laws expire before they can be addressed?**

In the mid-twentieth century, Congress began to include provisions in certain authorizing laws that explicitly authorized appropriations. When these explicit authorizations of appropriations were for set dollar amounts or were tied to specific fiscal years, this created an occasion for Congress to enact laws from time-to-time that revised and updated those provisions. At the same time, legislative efforts to “reauthorize” appropriations gave Congress an opportunity to conduct a broad legislative review and make needed policy changes.<sup>19</sup> In general, for programs subject to reauthorization, the two schedules of legislative review that emerged during this period were “annual” and “multiyear.” Annual authorizations of appropriations explicitly authorized appropriations for a single fiscal year, and necessitated legislative action to renew them every subsequent fiscal year. Multiyear authorizations of appropriations explicitly authorized appropriations for more than one fiscal year at a time (typically between two and five), and consequently required legislative action to renew those provisions on a less frequent basis.

Over the intervening decades, the number of agencies and programs that receive annual reauthorizations has waxed and waned.<sup>20</sup> Although the authorizing committees transitioned some new and existing agencies to annual authorizations at certain points in time, many of those agencies are now reauthorized less frequently. In some instances, the authorizing committees have chosen to only reauthorize certain aspects of an agency, or to reauthorize similar programs from multiple agencies simultaneously. Another avenue that the authorizing committees have taken is to transition certain annual reauthorization cycles to multiyear time periods. And in some cases, authorizations of appropriations (both annual and multiyear) lapsed for a number of fiscal years without being renewed.<sup>21</sup> There are a variety of reasons why authorizations of appropriations lapse and these vary according to context. For example, an authorizing committee might choose to defer action on a reauthorization if they determine that no programmatic changes are currently needed. Alternatively, reauthorization might not occur in a timely manner if there is a lack of congressional support for the program’s continuing existence. Or, there might be obstacles to

<sup>19</sup> For background on the development of these congressional rules and practices see Alan Schick, *Legislation, Appropriations, and Budgets: The Development of Spending Decision-making in Congress*, Congressional Research Service, May 1984; and Louis Fisher, “Annual Authorizations: Durable Roadblocks to Biennial Budgeting,” *Public Budgeting and Finance*, Spring 1983.

<sup>20</sup> For a further discussion, see CRS Report R43862, *Changes in the Purposes and Frequency of Authorizations of Appropriations*, by Jessica Tollestrup.

<sup>21</sup> The Congressional Budget Office (CBO) is required to compile this information each year under Section 202(e)(3) of the Congressional Budget Act. For FY1988, CBO identified a total of 45 laws with expired authorizations of appropriations (CBO, *Report on Unauthorized Appropriations and Expiring Authorizations*, January 15, 1988). That total grew to 256 such laws for FY2016 (CBO, *Unauthorized Appropriations and Expiring Authorizations*, January 15, 2016).

achieving congressional consensus regarding the programmatic changes that would be part of the debate on reauthorization.

The applicability of these reasons (and others not mentioned here) may vary as the congressional approach to the oversight and funding decision-making evolves over the years with regard to an agency or program. As a result, CRS is not able to generalize as to why some annual reauthorizations are enacted more consistently than others.

As of this current fiscal year, the only annual reauthorization to have been enacted each fiscal year over the course of its existence is the National Defense Authorization Act (NDAA).

The National Defense Authorization Act for Fiscal Year 2016 was the 54<sup>th</sup> consecutive annual defense authorization bill passed by Congress.<sup>22</sup> A confluence of factors may have contributed to the annual passing of defense authorization act, including the size and scope of the defense budget,<sup>23</sup> a history of bipartisan and bi-cameral focus on defense and national security issues,<sup>24</sup> and the culture and structure of the Armed Services Committees themselves. Current Armed Services Committee Chairmen John McCain and Mac Thornberry made reference to this culture in an October 22, 2015 op-ed in the *Wall Street Journal*, following the President's veto of the FY2016 NDAA (H.R. 1735).<sup>25</sup>

For more than 50 years Congress has fulfilled its highest constitutional duty to provide for the common defense by passing the National Defense Authorization Act, and year after year the NDAA has enjoyed broad, bipartisan support. Before Thursday, such bills had been vetoed by only four past Presidents, -in 1978, 1988, 1995 and 2007. In each case, the President objected to an actual provision in the bill, and each time Congress's Armed Services committees were able to find a compromise that earned the President's signature.

The NDAA legacy was upheld as the FY2016 NDAA was revised to comply with the revised funding limits set in the Bipartisan Budget Act of 2015,<sup>26</sup> and was signed into law by the President on November 25, 2015.<sup>27</sup>

Also contributing to success may be that the 50-year history of annually enacting an NDAA in and of itself sets an expectation with both congressional leadership and Members generally that enables continued annual consideration. The defense authorizing committees benefit from decades of experience and lessons learned regarding the production of an annual defense authorization bill despite changes in political party, House and Senate leadership, and committee members.<sup>28</sup> These experiences have led to clearly defined and established processes and protocols that enable the development and passage of annual authorization acts. Certain procedural steps are addressed through established committee protocols.<sup>29</sup> For example, the House Armed Services Committee has long required that any Member offering an amendment during committee mark-up of legislation must (1) obtain a waiver from the

<sup>22</sup> Congress passed the first "modern" NDAA for FY1962 as P.L. 87-53 ("To authorize appropriations for aircraft, missiles, and naval vessels for the Armed Forces, and for other purposes.") which was enacted on June 21, 1961.

<sup>23</sup> Honorable Mike McCord, *Defense Budget Overview - Fiscal Year 2017*, Under Secretary of Defense (Comptroller) and Chief Financial Officer, Pentagon, VA, February 9, 2017, <http://comptroller.defense.gov/BudgetMaterials.aspx>.

<sup>24</sup> Kevin McCarthy, House Majority Leader, "House Passes Bipartisan and Bicameral NDAA," press release, December 4, 2014, <http://kevinmccarthy.house.gov/media-center/press-releases/house-passes-bipartisan-and-bicameral-ndaa>.

<sup>25</sup> John and McCain, "Obama Vetoes His Own Military," *Wall Street Journal*, October 22, 2015.

<sup>26</sup> P.L. 114-74

<sup>27</sup> P.L. 114-92

<sup>28</sup> Pat Towell, "Congress and Defense," in *Congress and the Politics of National Security*, ed. David P. Auerswald and Colton C. Campbell (Cambridge, MA: Cambridge Press, 2012), p. 86-87.

<sup>29</sup> Colleen J. Shogan, *Like Clockwork: Senate Consideration of the National Defense Authorization Act*, Congressional Research Service, *CRS Centennial Series: The Evolving Congress*, Washington, DC, December 2014.

Chairman of the other House committees with jurisdiction on the matter; and (2) designate a source to offset any funding adjustments proposed by the amendment.<sup>30</sup> While not required by the Rules of the House, these committee protocols are intended to reduce the potential that the defense authorization bill could be subject to a point of order on the floor or be referred to other committees of jurisdiction in the House.

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<sup>30</sup> Transcript from House Armed Services Committee markup of the NDAA for FY2016.

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## **BUDGETING BLIND: THE UNRELIABILITY OF FEDERAL FINANCIAL DATA**

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**WEDNESDAY, APRIL 6, 2016**

U.S. SENATE,  
COMMITTEE ON THE BUDGET,  
*Washington, D.C.*

The Committee met, pursuant to notice, at 10:30 a.m., in Room SD-608, Dirksen Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Crapo, Johnson, Ayotte, Wicker, Perdue, Warner, Kaine, and King.

Staff Present: Eric Ueland, Republican Staff Director; Peter Warren, Senior Budget Analyst and Director of Oversight; for the Minority: Joshua Smith, Budget Policy Director.

### **OPENING STATEMENT OF CHAIRMAN ENZI**

Chairman ENZI. Good morning, and since we are here, I will go ahead and call this hearing to order.

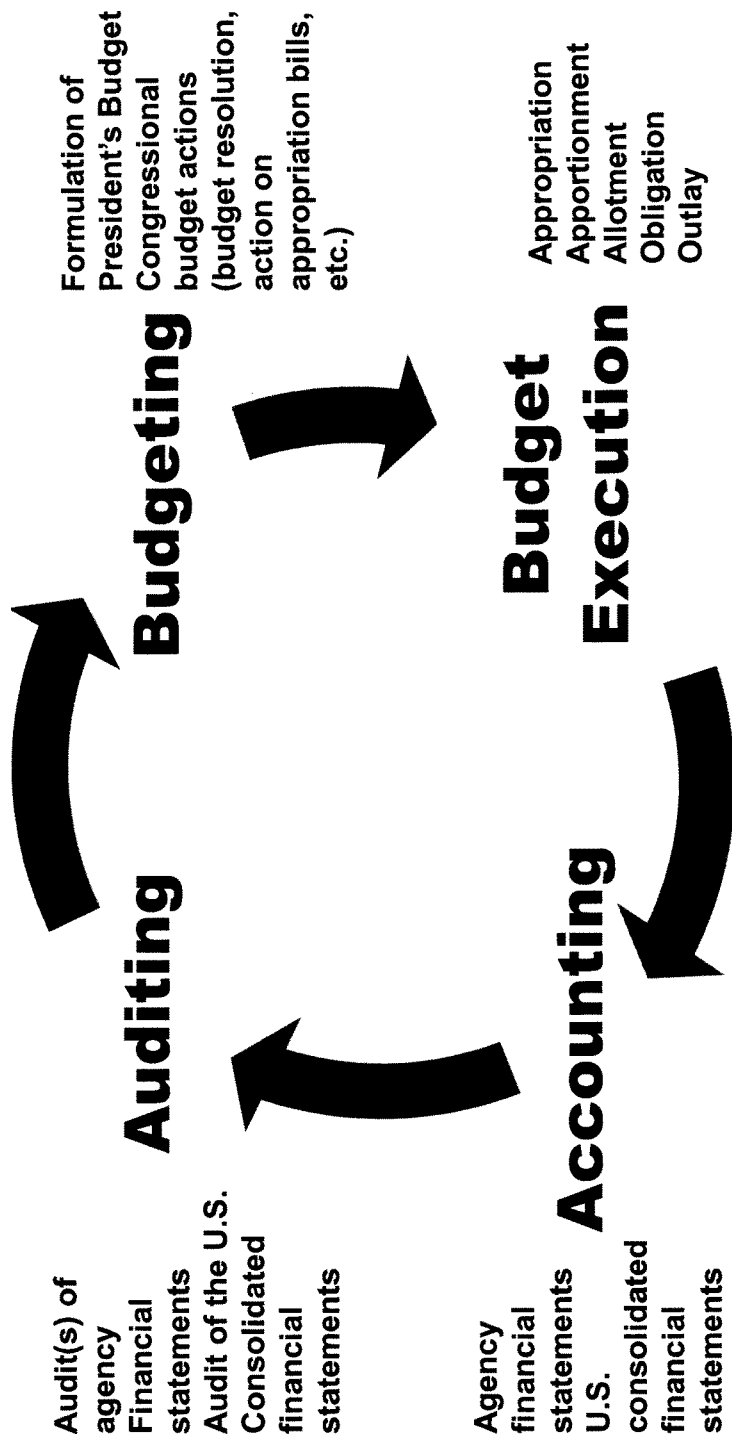
Today we are going to begin a series of hearings that will discuss budget process reform in what I anticipate will be a positive, productive, and bipartisan manner. I think this is one of the few times that we can do that. It is an opening once every 4 years, and the reason it is an opening every 4 years is right now we do not know who the majority is going to be next year; we do not know who the President is going to be next year. So I anticipate that both sides can work in a very reasonable way to make a process that will be better than what we have had before.

So we begin today with an assessment of the Government's overall financial condition. The lens through which we will assess that condition is the Government Accountability Office's recent audit of the Federal Government's financial books.

As you know, I believe the congressional budget process is fundamentally broken. Only one budget resolution has been adopted by Congress in the past 6 years, and only nine budgets have been adopted in the past 18 years. Even when we do adopt a budget, it often fails to become a governing document. The broken budget process has contributed to spiraling levels of overspending and debt. But it is important to understand that the budget process is just one part of a broader cycle of Federal financial management.

The cycle is shown on the slide that you can see on the screen. As you can see, this continuous cycle proceeds from budgeting through budget execution to accounting and on to auditing. All the elements are interrelated. Judging from testimony we will hear today from the Government Accountability Office, the budget proc-

ess is not the only part of this cycle that is broken. The government-wide financial statements that GAO audits tell us what came into the Government's coffers and what went out, what the Government owns and what it owes, and if the operations are financially sustainable.



Source: CRS

But can we trust the information in the financial statements? GAO's audit calls into question the reliability of the underlying financial data. The sketchiness is such that GAO remains unable to even issue an audit opinion on the Government's books. If a publicly owned company on the stock market received such a disclaimer, investors would run away from it. But we cannot run away from a Government in which we are all stakeholders. This is an enterprise in which we and our children are all invested.

It would be disastrous for a publicly owned company to be unable to prove to auditors that it had a handle on how much inventory was held in its own warehouses, what condition its property was in, or the extent to which it is on the hook for potential liabilities. But these are exactly the sort of weaknesses GAO found in the Federal Government books. The situation has implications for budgeteers because it means we may not have the most reliable data when we embark on the budgeting stage of the financial management cycle.

This is how GAO puts it in its report: "To make difficult decisions to address the Federal Government's fiscal challenges, Congress, the administration, and Federal managers must have ready access to reliable and complete financial and performance information. Our report underscores that much work remains to improve Federal financial management, and these improvements are urgently needed."

The tendency in Congress is to focus on all the wonderful things that new spending and new programs might accomplish. There is not enough interest in looking at what happens with the money we are already spending. That is where the audits come in. Every budget should be informed by knowledge about what happened with the money that already went out the door. To wisely allocate new resources, we need to be using reliable information about what we bought, what we own, where we stand, and the sustainability of the current policies.

Ultimately, I hope this hearing will encourage better stewardship by the financial managers within the executive branch. As Congress works to fix its broken budget, it is clear the administration has its own work to do in getting its financial house in order.

Senator Warner.

#### **OPENING STATEMENT OF SENATOR WARNER**

Senator WARNER. Well, thank you, Mr. Chairman. Thank you for holding this important hearing.

Comptroller Dodaro, it is great to see you again. I am looking forward to your testimony.

I think there is some self-selection going on in terms of who showed up. We have got your background as an accountant, Mr. Chairman, and Senator Grassley's interest. We have got three former business guys who decided to show up this morning. While this is not necessarily an area that gets a lot of attention, it is extraordinarily important, and I agree with the Chairman on this.

We have made some progress. You know, back in 2010, working with your offices, we passed GPRA, the first effort to try to modernize the management process, where we looked at trying to iso-

late the actual priorities for agencies, looking at cross-cutting goals across agencies, looking at consolidation.

In 2014—and, again, I appreciate your comments, Mr. Dodaro, about the DATA Act, at least a first step. Rob Portman and I and Darrell Issa put the DATA Act in place to try to start consolidating so we can have that kind of clarity around financial information. I do hope this Congress goes ahead and invests the \$53 million that the President has called for to actually implement it. It does not do any good to pass this legislation if we cannot implement its processes.

You know, I think one of the things in your testimony, we are talking about both improving Federal finances both in the long term and financial management. An issue that many of us share a great deal of concern on is, obviously, our national debt, which is approaching \$19 trillion. A data point I always like to use is at interest rates go up, just 100 basis points, 1 percent, that adds \$120 billion a year in just additional debt service. That is more than we spend in Federal DOE and DHS combined. I know the Chairman of the Homeland Security Committee is here.

Another issue I think you pointed out and something that we have been working on as well is the unrecognized financial risk posed by the ongoing Government conservatorship of Fannie and Freddie. This is an area that has not garnered a lot of attention, but as we have seen potential for either one of those entities to dip back in and ask the taxpayer, again, we have got to—our job is to make sure that we resolve those entities.

I would point out to Treasury and the OMB, I think there are challenges with this administration, but the requirement to put in place a consolidated financial report has been part of the law since 1994. And, unfortunately, as your report points out, we still do not have good systems in place, particularly around the issue of inter-governmental transfers. So if we cannot follow the money, as the Chairman has pointed out, we are not going to be able to do our job in terms of oversight.

In 2012, a GAO report found that the Pentagon alone maintains more than 2,200 systems to manage finances, HR, logistics, property, and weapons acquisition. I have run an enterprise before. Obviously, DOD is the largest in the world, but 2,200 separate systems? That is crazy.

One last comment I want to make in terms of another area that I know the Comptroller General has pointed out is around cyber. I think this is going to be a growing concern, public and private. But our failure at times to actually invest in, improve our legacy IT systems, we are now seeing a new vulnerability not only in terms of inability for these systems to work, but as we patch upon patch upon patch, all we are doing is creating more vulnerabilities in terms of this new domain around cyber.

I would simply point out, finally, that if we are going to make sure that we do the kind of oversight and review when we get to program integrity, we have got to make sure we fund those initiatives. These return in many cases \$8 to \$10 in savings for every \$1 invested, and I worry at times when we go through things like sequestration, which makes no regard for good programs or bad programs, program integrity initiatives, because they fall within

the discretionary bucket, are all subject to those kinds of caps and those kinds of cuts.

So, Mr. Chairman, I am grateful for your focus on this issue. It is something I think there is bipartisan consensus on. My hope would be we could get more members of the Committee to participate, and I look forward to the proceeding and the testimony of our witness.

Chairman ENZI. Thank you, and thank you for your work on the DATA Act. And I thank you and Senator Kaine and Senator Johnson and Senator Perdue and a number of people for talking about the need for separating out the capital budget from the normal expenditures and seeing what things we borrow for.

I am glad we are doing this hearing today because we are used to looking at Federal finances through the lens of the budget resolution. This hearing gives us a different perspective. It is not often, for instance, that we look at the actual balance sheet of the Federal Government. One thing that jumps off the page for me in viewing that balance sheet is the growth of Federal banking operations. The Government's largest asset class is its \$1.2 trillion loan portfolio. That is 38 percent of everything the Government owns. The student loan portfolio alone is nearly \$1 trillion, and that is more than the combined value of all Federal property, plant, and equipment.

Our witness today is Gene Dodaro, the Comptroller General of the Government Accountability Office. GAO is statutorily responsible for auditing the consolidated government-wide financial statements. He is the eighth Comptroller General of the United States. He was confirmed in December of 2010 after serving as Acting Comptroller General since March of 2008. He has been with the GAO for more than 40 years. He served 9 years as the Chief Operating Officer, the number two leadership position at the agency. Prior to that, he headed the GAO's Accounting and Information Management Division, which specialized in financial management, computer technology, and budget issues. He testified before this Committee last year on the topic of duplicative programs.

I thank you for joining us again today to discuss GAO's most recent annual audit of the Government's books. Mr. Dodaro.

**STATEMENT OF THE HONORABLE GENE L. DODARO, COMPTROLLER GENERAL OF THE UNITED STATES, U.S. GOVERNMENT ACCOUNTABILITY OFFICE**

Mr. DODARO. Thank you very much, Mr. Chairman, Senator Warner, Senators Johnson, Grassley, and Crapo. Good morning to all of you. I am very pleased to be here to discuss the audit that we perform on the Government's financial report.

As has been pointed out in the opening comments, the financial report does not get anywhere near the attention that the budget does, but it is really needed to provide a total perspective on the Government's financial condition and position.

First of all, it provides a good insight into the accountability over the money that has been spent already and the proper stewardship over assets that the Government owns. It provides more insights into fiscal exposures and insurance programs and environmental liabilities that are not included in the budget process. And since sus-

tainability financial statements have been added, it provides a long-term perspective on the Federal Government's current fiscal path, which I think is an important area to focus on, and I will talk a little bit about that in my comments this morning.

There are just four basic points I would like to make in my opening statement.

Number one, there has been some progress in improving financial management in the Federal Government over the past 20 years; however, significant problems remain. There are three major impediments to our ability to give the Government financial statements an audit opinion. Serious financial management problems at DOD, which reportedly has assets that are about 30 percent of the total Government assets and about 15 percent of its net costs. These are serious, longstanding problems that need to be addressed.

Secondly, Treasury cannot eliminate, along with the other agencies, the intragovernmental transactions that Senator Warner pointed out in his comments among Federal agencies. These are hundreds of billions of dollars in transactions, so you really do not have good accountability on how the Federal agencies take the appropriations from the Congress agency by agency, but then carry out business activities among themselves, and there needs to be a proper accounting for that money.

And, finally, there are problems compiling the financial statements. Most of the individual Federal agencies are able to get unmodified or clean opinions, and that has been a significant improvement since 1996 when the federal government first started producing audited financial statements for all the major departments and agencies in the Federal Government. In 1996, only six departments and agencies could get unmodified (clean opinions); most recently 21 of 24 have been able to do that. But some of the big agencies like DOD have been problematic.

Secondly, the financial report and audit shines light on some significant government-wide financial challenges. Number one is improper payments. Since Congress has required the reporting on the estimates of improper payments in 2003, the amount of improper payment estimates now exceed \$1 trillion. This is a significant problem. In the last 3 years alone, the annual figures have grown, from \$105 billion to \$124 billion to \$136 billion. It is a pervasive problem across Government; 121 different Federal programs and 22 Federal agencies are reporting improper payments. The most significant improper payments are in Medicare and Medicaid, two of the fastest growing programs in the Federal Government's inventory. So this is something that I believe really needs to have attention.

On the other side of the equation, while we have some money going out the door that perhaps should not be going out the door, we have a net tax gap of taxes that are owed under the current system but not being paid. The latest estimate is \$385 billion. So there is a significant amount of money under the current laws and programs that we do not have proper accountability over and we are not properly collecting all the revenues due to the Federal Government.

The third major point that I would make is that, while there has been some progress in the past few years in reducing the annual deficit, the Federal Government remains on a long-term unsustainable fiscal path. The debt-to-GDP ratio right now is at 74 percent. That is the highest it has been since World War II when we had a record 106 percent of debt held by the public as a percent of gross domestic product. And we are on a path to exceed those historical numbers in 15 to 25 years absent fiscal policy changes. Key drivers are demographics and rising health care costs, and eventually net interest. As net interest accumulates, compound interest works against us when we are borrowing, not for us as it would when saving.

The last point I would make is that the current approach to setting a debt ceiling for the Federal Government in my opinion needs to be revised. The concerns about whether the Congress will raise the debt ceiling has caused the Treasury markets to take actions. Market participants are actually avoiding purchasing Treasuries that might mature during the debt ceiling impasse and it is causing liquidity problems in the secondary market, and it is adding to the interest that the Federal Government has to pay on the debt. Our latest estimate for the 2013 debt ceiling impasse was the Federal Government paid anywhere from \$38 to \$70 million in additional interest costs just because people were concerned. Some of the market participants that we talked to basically said that they might take more severe action in the future.

So we have recommended that Congress change the approach for setting the debt ceiling. It could be done as part of the budget resolution process, but it needs to be brought closer to where the actual spending decisions are made by the Federal Government. Under the current approach, raising the debt ceiling authorizes Treasury to borrow money to pay bills that the Congress has already authorized to be paid. It does not control anything with regard to the revenue or spending activities of the Federal Government.

So I would encourage this Committee, as you consider budget process reforms, to include in that discussion alternative ways of setting the debt ceiling for the Congress.

I appreciate the opportunity to discuss GAO's work on these issues, Mr. Chairman, and I would be happy to answer any questions that you and other members of the Committee may have.

[The prepared statement of Mr. Dodaro follows:]





United States Government Accountability Office

Testimony  
Before the Committee on the Budget,  
U.S. Senate

For Release on Delivery  
Expected at 10:30 a.m. ET  
Wednesday, April 6, 2016

# FISCAL YEAR 2015 U.S. GOVERNMENT FINANCIAL STATEMENTS

## Need to Address the Government's Remaining Financial Management Challenges and Long- Term Fiscal Path

Statement of Gene L. Dodaro  
Comptroller General of the United States

## GAO Highlights

Highlights of GAO-16-541T, a testimony before the Committee on the Budget, U.S. Senate

April 6, 2016

### FISCAL YEAR 2015 U.S. GOVERNMENT FINANCIAL STATEMENTS:

#### Need to Address the Government's Remaining Financial Management Challenges and Long-Term Fiscal Path

#### Why GAO Did This Study

Congress and the President need reliable, useful, and timely financial and performance information to make difficult budget choices and deal with the nation's long-term fiscal challenges. To determine if this need is met, among other things GAO annually audits the governmentwide financial statements contained in the *Financial Report*.

Taken together, the *Financial Report* and the *Budget of the United States Government (Budget)* are complementary documents that provide a comprehensive perspective on the government's financial position and condition. The *Budget* accounts for government receipts, or cash received by the government, and spending (outlays), or payments made by the government to the public. The *Financial Report* includes the governmentwide financial statements, presenting the government's revenues and costs, assets and liabilities, and sustainability reporting, and discusses other important financial information.

This testimony discusses the federal government's remaining financial management challenges and long-term fiscal path, specifically in the context of GAO's report on the fiscal year 2015 governmentwide financial statements.

#### What GAO Recommends

Over the years, GAO has made numerous recommendations directed at improving federal financial management. The federal government has generally taken or plans to take actions to address GAO's recommendations.

View GAO-16-541T. For more information, contact Robert F. Dacey, [daceyrf@gao.gov](mailto:daceyrf@gao.gov) or J. Lawrence Malenich, [malenichj@gao.gov](mailto:malenichj@gao.gov) or (202) 512-3406; and J. Christopher Mihm, [mihmj@gao.gov](mailto:mihmj@gao.gov) or (202) 512-6806.

#### What GAO Found

The *Financial Report of the U.S. Government (Financial Report)* provides important information to the Congress, federal agencies, and the public, including the government's financial condition and the reliability of data used to help support budget and financial decisions. While significant progress has been made in improving federal financial management over the past 20 years, material weaknesses in internal control over financial reporting and other limitations continued to prevent GAO from expressing an opinion on the government's accrual-based financial statements. Three major impediments are: (1) serious financial management problems at DOD, which represented 30 percent and 15 percent of the government's reported total assets and net costs, respectively; (2) the government's inability to adequately account for and reconcile a significant amount of intragovernmental activity and balances between federal entities, which resulted in hundreds of billions of dollars in differences; and (3) the government's ineffective process for preparing the U.S. government's consolidated financial statements (governmentwide financial statements).

Unless these weaknesses are adequately addressed, they will, among other things, continue to (1) hamper the government's ability to reliably report a significant portion of its assets, liabilities, costs, and other related information; and (2) hinder the government from having reliable financial information to operate in an efficient and effective manner. Efforts are under way to resolve these issues, but strong and sustained commitment by DOD and other federal entities, as well as continued leadership by Treasury and OMB, are needed.

The *Financial Report* also helps to convey the long-term fiscal position of the federal government. However, significant uncertainties, primarily related to the achievement of projected reductions in Medicare cost growth, and a material weakness in internal control over financial reporting prevented GAO from expressing an opinion on the sustainability financial statements, including the new Statement of Long-Term Fiscal Projections. The sustainability financial statements are critical to understanding the government's financial condition and sustainability of current fiscal policies. Although the timing and size of the increase in debt as a share of gross domestic product varies depending on the assumptions used, both the long-term fiscal projections included in the governmentwide financial statements and GAO's own recent long-term fiscal simulations show that absent policy changes, the federal government continues to face an unsustainable long-term fiscal path.

Other challenges that need urgent attention are highlighted in the *Financial Report*, including (1) the significant and pervasive government-wide issue of improper payments, which totaled over \$1 trillion since fiscal year 2003, and (2) reducing the annual net tax gap, last estimated by IRS to be \$385 billion.

Finally, GAO has identified ways that Congress could consider for better linking decisions about the debt limit with decisions about spending and revenue at the time those decisions are made. These potential approaches would both achieve this link and minimize disruptions to the market.

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Chairman Enzi, Ranking Member Sanders, and Members of the Committee:

I appreciate the opportunity to be here today to discuss the need to address the federal government's remaining financial management challenges and long-term fiscal path. My statement is framed in the context of our report on the U.S. government's fiscal year 2015 consolidated financial statements (governmentwide financial statements), which is included in the *Financial Report of the United States Government (Financial Report)*.

In passing a series of financial management reform legislation in the 1990s, Congress sought to address the historical lack of reliable, useful, and timely information to assure financial accountability for the federal government. Such legislation included the Chief Financial Officers (CFO) Act of 1990, as expanded by the Government Management Reform Act of 1994 (GMRA), which requires the inspectors general of the 24 CFO Act agencies to be responsible for annual audits of agency-wide financial statements prepared by these entities, beginning with fiscal year 1996.<sup>1</sup> GMRA also requires the preparation of annual financial statements covering the executive branch of the government, beginning with financial statements prepared for fiscal year 1997.<sup>2</sup> Treasury and OMB have elected to include certain financial information on the legislative and judicial branches in the governmentwide financial statements as well. GAO is responsible for the audit of the governmentwide financial statements.<sup>3</sup> Further, with the enactment of the Accountability of Tax Dollars Act of 2002 (ATDA), most executive branch entities must now annually prepare financial statements and have them audited.<sup>4</sup>

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<sup>1</sup>31 U.S.C. § 3521(e). GMRA authorized the Office of Management and Budget to designate agency components that also would receive financial statement audits. See 31 U.S.C. § 3515(c).

<sup>2</sup>31 U.S.C. § 331(e)(1). GMRA requires the Secretary of the Treasury, working in coordination with the Director of OMB, to annually submit to the President and Congress audited financial statements covering the executive branch.

<sup>3</sup>GMRA, Pub. L. No. 103-356, § 405(c), 108 Stat. 3410, 3416-17 (Oct. 13, 1994), *codified at* 31 U.S.C. § 331(e)(2).

<sup>4</sup>ATDA, Pub. L. No. 107-289, 116 Stat. 2049 (Nov. 7, 2002), *codified at* 31 U.S.C. § 3515.

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During fiscal year 2015, the federal government's reported unified budget deficit decreased by about \$45 billion to approximately \$439 billion. However, the federal government continues to face an unsustainable long-term fiscal path. To operate as effectively and efficiently as possible and to make difficult decisions to address the federal government's fiscal challenges, Congress, the administration, and federal managers must have ready access to reliable, useful, and timely financial and performance information—both for individual federal entities and for the federal government as a whole. Reliable financial information would also be helpful as you face the difficult budget choices needed to deal with our long-term fiscal outlook. Also, without reliable, useful, and timely financial information, the government cannot adequately ensure accountability over spending and its assets, accurately measure and control costs, manage for results, or make timely and fully informed decisions about allocating limited resources.

Taken together, the *Financial Report* and the *Budget of the United States Government (Budget)* are complementary documents that provide a comprehensive perspective on the federal government's financial position and condition. The *Budget* is the government's primary financial planning and control tool. It also accounts for past government receipts and spending. The *Budget* focuses on receipts, or cash received by the federal government, and outlays, or payments made by the federal government to the public.

The *Financial Report* includes the governmentwide financial statements, consisting of the accrual-based financial statements,<sup>5</sup> the sustainability financial statements,<sup>6</sup> the related notes to these financial statements, as well as other important financial information. The accrual-based financial

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<sup>5</sup>The accrual-based financial statements as of and for the fiscal years ended September 30, 2015, and 2014, consist of the (1) Statements of Net Cost, (2) Statements of Operations and Changes in Net Position, (3) Reconciliations of Net Operating Cost and Unified Budget Deficit, (4) Statements of Changes in Cash Balance from Unified Budget and Other Activities, and (5) Balance Sheets, including the related notes to these financial statements. Most revenues are recorded on a modified cash basis.

<sup>6</sup>The sustainability financial statements comprise the Statement of Long-Term Fiscal Projections, covering all federal government programs, and the Statement of Social Insurance and the Statement of Changes in Social Insurance Amounts, covering social insurance programs (Social Security, Medicare, Railroad Retirement, and Black Lung programs). The sustainability financial statements do not interrelate with the accrual-based financial statements.

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statements present historical information on what the federal government owns (assets) and owes (liabilities) at the end of the year, what came in (revenues—amounts earned, but not necessarily collected) and what went out (net costs—amounts incurred, but not necessarily paid) during the year, and how accrual-based net operating costs of the federal government reconcile to the budget deficit and changes in its cash balances during the year.

The sustainability financial statements are designed to illustrate the relationship between projected receipts and expenditures if current policy is continued over a 75-year time horizon. For this purpose, the projections assume that scheduled social insurance benefit payments would continue after related trust funds are projected to be exhausted, contrary to current law, and that debt could continue to rise indefinitely without severe economic consequences. The sustainability financial statements are intended to help readers understand current policy and the importance and magnitude of policy reforms necessary to make it sustainable.<sup>7</sup>

The objectives of financial reporting are designed to enhance the financial information reported by the federal government to (1) demonstrate the federal government's accountability and provide useful information to internal and external users of federal financial reports, and (2) help internal users of financial information improve the government's management.

Overall, significant progress has been made in improving federal financial management since the enactment of key federal financial management reforms in the 1990s; however, our report on the governmentwide financial statements underscores that much work remains to improve federal financial management, and these improvements are urgently needed. Congressional oversight is critical to ensuring continued progress. The annual audits of the agency and governmentwide financial statements are an independent assessment of the reliability of the information contained in such financial statements and are a key element

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<sup>7</sup>By accounting convention, the Statement of Social Insurance does not include projected general revenues that, under current law, would be used to finance the remainder of the expenditures in excess of revenues for Medicare Parts B and D reported in the Statement of Social Insurance. The Statement of Long-Term Fiscal Projections includes all revenues (including general revenues) of the federal government.

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in providing accountability over the federal government's finances and assets.

Our testimony today discusses the following major issues that are highlighted in the *Financial Report*.

- the overall results of our recent audit of the fiscal year 2015 governmentwide financial statements;
- accrual costs incurred by the federal government and certain financial risks that could affect the federal government's financial condition in the future;
- challenges posed by the federal government's long-term fiscal outlook; and
- improving the link between policy decisions that create debt and the authority to borrow (the debt limit) at the time those decisions are made.

In February, we reported on the results of our audit of the fiscal year 2015 governmentwide financial statements.<sup>8</sup> Both the financial statements and our related audit report are included in the 2015 Financial Report.<sup>9</sup> We performed sufficient audit work to provide our reports on the financial statements; internal control over financial reporting; and compliance with laws, regulations, contracts, and grant agreements. We conducted our audit in accordance with U.S. generally accepted government auditing standards. Our audit report would not be possible without the commitment and professionalism of inspectors general throughout the federal government who are responsible for annually auditing the financial statements of individual federal entities.

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<sup>8</sup>GAO-16-357R.

<sup>9</sup>The 2015 *Financial Report*, which is an enclosure to GAO-16-357R, is available through the Department of the Treasury at [https://www.fiscal.treasury.gov/fsreports/rpt/finrep/fr/fr\\_index.htm](https://www.fiscal.treasury.gov/fsreports/rpt/finrep/fr/fr_index.htm). Also, see GAO, *Understanding the Primary Components of the Annual Financial Report of the United States Government*, GAO-09-946SP (Washington, D.C.: September 2009).

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**Overall Results of  
Our Audit**

I would like to discuss (1) material weaknesses and other limitations that prevented us from providing an opinion on the accrual-based financial statements, (2) efforts to address major impediments to an opinion on the accrual-based financial statements, (3) other material weaknesses that contributed to the government's ineffective internal control over financial reporting, and (4) significant uncertainties and a material weakness that prevented us from providing an opinion on the sustainability financial statements.

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**Material Weaknesses in  
Internal Control over  
Financial Reporting and  
Other Limitations Resulted  
in a Disclaimer of Opinion  
on the Accrual-Based  
Financial Statements**

The federal government was unable to demonstrate the reliability of significant portions of its accrual-based financial statements as of and for the fiscal years ended September 30, 2015, and 2014, principally resulting from limitations related to certain material weaknesses in internal control over financial reporting<sup>10</sup> and other limitations affecting the reliability of these financial statements. For example, about 34 percent of the federal government's reported total assets as of September 30, 2015, and approximately 19 percent of the federal government's reported net cost for fiscal year 2015, relate to three CFO Act agencies—the Department of Defense (DOD), the Department of Housing and Urban Development, and the U.S. Department of Agriculture—that received disclaimers of opinion on their fiscal year 2015 financial statements. As a result, we were prevented from providing an opinion on the accrual-based financial statements.

The federal government did not maintain adequate systems or have sufficient appropriate evidence to support certain material information reported in its accrual-based financial statements. The underlying material weaknesses in internal control, which have existed for years, contributed to our disclaimer of opinion on the accrual-based financial statements as of and for the fiscal years ended September 30, 2015, and

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<sup>10</sup>A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

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2014.<sup>11</sup> Specifically, these weaknesses concerned the federal government's inability to

- satisfactorily determine that property, plant, and equipment and inventories and related property, primarily held by DOD, were properly reported in the accrual-based financial statements;
- reasonably estimate or adequately support amounts reported for certain liabilities, such as environmental and disposal liabilities, or determine whether commitments and contingencies were complete and properly reported;
- support significant portions of the reported total net cost of operations, most notably related to DOD, and adequately reconcile disbursement activity at certain federal entities;
- adequately account for and reconcile intragovernmental activity and balances between federal entities;
- reasonably assure that the governmentwide financial statements are (1) consistent with the underlying audited entities' financial statements, (2) properly balanced, and (3) in accordance with U.S. generally accepted accounting principles (U.S. GAAP); and
- reasonably assure that the information in the (1) Reconciliations of Net Operating Cost and Unified Budget Deficit and (2) Statements of Changes in Cash Balance from Unified Budget and Other Activities is complete and consistent with the underlying information in the audited entities' financial statements and other financial data.

These material weaknesses continued to (1) hamper the federal government's ability to reliably report a significant portion of its assets, liabilities, costs, and other related information; (2) affect the federal government's ability to reliably measure the full cost as well as the financial and nonfinancial performance of certain programs and activities; (3) impair the federal government's ability to adequately safeguard significant assets and properly record various transactions; and (4) hinder

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<sup>11</sup>A detailed description of the material weaknesses that contributed to our disclaimer of opinion, including the primary effects of these material weaknesses on the accrual-based financial statements and on the management of federal government operations, can be found on pp. 257 through 262 of the *2015 Financial Report*.



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the federal government from having reliable financial information to operate in an efficient and effective manner.

It is important to note, however, that since the enactment of key federal financial management reforms in the 1990s, significant progress has been made in improving federal financial management activities and practices. For fiscal year 2015, almost all of the 24 CFO Act agencies received unmodified ("clean") audit opinions on their respective entities' financial statements, up from 6 CFO Act agencies for fiscal year 1996.<sup>12</sup> In addition, accounting and financial reporting standards have continued to evolve to provide greater transparency and accountability over the federal government's operations, financial condition, and fiscal outlook. Further, the preparation and audit of individual federal entities' financial statements have identified numerous deficiencies, leading to corrective actions to strengthen federal entities' internal controls, processes, and systems. However, many of the CFO Act agencies continue to struggle with financial management systems that do not meet the needs of management for reliable, useful, and timely financial information.

The Federal Financial Management Improvement Act of 1996 (FFMIA) was designed to lead to system improvements that would result in CFO Act agency managers routinely having access to reliable, useful, and timely financial-related information with which to measure performance and increase accountability throughout the year.<sup>13</sup> FFMIA requires auditors, as part of the 24 CFO Act agencies' financial statement audits, to report whether those agencies' financial management systems substantially comply with (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) the federal government's *U.S. Standard General Ledger* at the transaction level.

For fiscal year 2015, auditors at 12 of the 24 CFO Act agencies reported that the agencies' financial management systems did not substantially comply with one or more of the three FFMIA requirements. Long-standing

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<sup>12</sup>See app. I for the fiscal year 2015 audit results for the 24 CFO Act agencies.

<sup>13</sup>FFMIA, which is reprinted in 31 U.S.C. § 3512 note, defines "financial management systems" to include the financial systems and the financial portions of mixed systems necessary to support financial management, including automated and manual processes, procedures, controls, data, hardware, software, and support personnel dedicated to the operation and maintenance of system functions.

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	<p>financial management systems weaknesses at several large CFO Act agencies, along with the size and complexity of the federal government, continue to present a formidable management challenge in providing accountability to the nation's taxpayers and have contributed significantly to certain of the material weaknesses and other limitations discussed in our audit report. Therefore, it is important for the individual federal entities to remain committed to maintaining the progress that has been achieved in obtaining positive audit results and to build upon that progress to make needed improvements in federal financial management systems.</p>
<b>Efforts to Address Impediments to an Opinion on the Accrual-Based Financial Statements</b>	<p>Three major impediments continued to prevent us from rendering an opinion on the government's accrual-based financial statements: (1) serious financial management problems at DOD that have prevented its financial statements from being auditable, (2) the federal government's inability to adequately account for and reconcile intragovernmental activity and balances between federal entities, and (3) the federal government's ineffective process for preparing the governmentwide financial statements.</p>
<b>Improving Financial Management at DOD</b>	<p>Having sound financial management practices and reliable, useful, and timely financial information is important to ensure accountability over DOD's extensive resources to efficiently and economically manage the department's assets, budgets, mission, and operations. Accomplishing this goal is a significant challenge given the worldwide scope of DOD's mission and operations; the diversity, size, and culture of the organization; and its reported trillions of dollars of assets and liabilities and its hundreds of billions of dollars in annual appropriations. Given the federal government's continuing fiscal challenges, reliable, useful, and timely financial and performance information is important to help federal managers ensure fiscal responsibility and demonstrate accountability. This is particularly true for DOD, the federal government's largest department—which represented about 30 percent of the federal government's reported total assets as of September 30, 2015, and approximately 15 percent of the federal government's reported net cost for fiscal year 2015.</p> <p>DOD continues to work toward the long-term goal of improving financial management and auditability of its department-wide financial statements. The National Defense Authorization Act (NDAA) for Fiscal Year 2010</p>

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requires that DOD's Financial Improvement and Audit Readiness (FIAR) Plan<sup>14</sup> set as its goal that the department's financial statements be validated as ready for audit by September 30, 2017.<sup>15</sup>

DOD's current FIAR strategy and methodology focus on two priorities—budgetary information and asset accountability—with an overall goal of preparing auditable department-wide financial statements by September 30, 2017. Based on difficulties encountered in preparing for an audit of the Statement of Budgetary Resources (SBR), DOD made a significant change to its FIAR Guidance that limited the scope of the first-year SBR audits for all DOD components.<sup>16</sup> As outlined in the November 2014 FIAR Plan Status Report and the November 2013 revised FIAR Guidance, the scope of initial SBR audits beginning in fiscal year 2015 was to focus on current-year budget activity, to be reported on a Schedule of Budgetary Activity (SBA).<sup>17</sup> This was intended to be an interim step toward achieving

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<sup>14</sup>DOD's FIAR Plan is a strategic plan and management tool for guiding, monitoring, and reporting on the department's ongoing financial management improvement efforts and for communicating the department's approach to addressing its financial management weaknesses and achieving financial statement audit readiness. The FIAR Plan was last updated in November 2015.

<sup>15</sup>Section 1003 of the National Defense Authorization Act for Fiscal Year 2010, Pub. L. No. 111-84, 123 Stat. 2190, 2439-41 (Oct. 28, 2009), made the development and maintenance of the FIAR Plan a statutory requirement. Under the act, the FIAR Plan must describe specific actions to be taken and the costs associated with ensuring that DOD's financial statements are validated as ready for audit by September 30, 2017. In addition, section 1005 of the National Defense Authorization Act for Fiscal Year 2013, Pub. L. No. 112-239, 126 Stat. 1632, 1904-05 (Jan. 2, 2013), enacted a requirement for DOD's FIAR Plan to describe specific actions to be taken and the costs associated with ensuring that one of DOD's financial statements, the Statement of Budgetary Resources, would be validated as ready for audit by September 30, 2014, but DOD has acknowledged that it did not meet this target date. More recently, the National Defense Authorization Act for Fiscal Year 2014 also mandated an audit of DOD's fiscal year 2018 financial statements, and that those results be submitted to Congress by March 31, 2019. Pub. L. No. 113-66, div. A, § 1003, 127 Stat. 672, 842 (Dec. 26, 2013) (*reprinted in* 10 U.S.C. § 2222 note).

<sup>16</sup>The FIAR Guidance was first issued by the DOD Comptroller in May 2010 and provides a standardized methodology for DOD components to follow for achieving financial management improvements and auditability. The DOD Comptroller periodically updates this guidance, most recently in April 2015.

<sup>17</sup>Unlike the SBR, which reflects multiple-year budget activity, the SBA reflects the balances and associated activity related only to funding from fiscal year 2015 forward. As a result, the SBAs will exclude unobligated and unexpended amounts carried over from funding prior to fiscal year 2015, as well as information on the status and use of such funding (e.g., obligations incurred and outlays) in fiscal year 2015 and thereafter.

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the audit of multiple-year budgetary activity required for an audit of the SBR. In making this strategic change, DOD officials concluded—based on the difficulties encountered in obtaining documentation for prior year transactions on the U.S. Marine Corps SBR audit—that the most effective path to an audit of the SBR would be to start with reporting and auditing only current-year activity for fiscal year 2015 appropriations and expanding subsequent audits to include current-year appropriations and prior appropriations going back to fiscal year 2015.

Consequently, certain DOD components—including the Army, Navy, and Air Force—underwent their first SBA audits for fiscal year 2015. Independent public accountants (IPA) issued disclaimers of opinion on the Army's, Navy's, and Air Force's fiscal year 2015 SBAs,<sup>18</sup> and identified material weaknesses in internal control at all three military departments. Army, Navy, and Air Force management have generally concurred with the findings in the respective IPA reports and stated that they will develop and execute corrective actions to address the IPAs' recommendations. In its November 2015 FIAR Plan Status Report, DOD reported that the Army, Navy, and Air Force will again undergo SBA audits for fiscal year 2016.

To meet its goal of having its department-wide financial statements audit ready by September 30, 2017,<sup>19</sup> DOD developed seven critical path milestones and dates by which those milestones have to be completed. For example, DOD has identified reconciling Fund Balance with Treasury<sup>20</sup> and valuation of assets (e.g., general property, plant, and equipment and inventory and related property) as critical to its efforts to

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<sup>18</sup>The Air Force's IPA issued its opinion on November 20, 2015, the Army's IPA issued its opinion on January 15, 2016, and the Navy's IPA issued its opinion on February 29, 2016.

<sup>19</sup>Per the FIAR plan, "audit ready" means the department has strengthened internal controls and improved financial practices, processes, and systems so there is reasonable confidence that the information can undergo an audit by an independent auditor. To undergo an audit does not necessarily mean that the department is representing that it will receive an unmodified opinion on the information being audited, but rather that there is a reasonable basis for an independent auditor to audit the information.

<sup>20</sup>In the federal government, an agency's Fund Balance with Treasury accounts are similar in concept to corporate bank accounts. The difference is that instead of a cash balance, Fund Balance with Treasury represents unexpended spending authority in appropriation accounts. Similar to bank accounts, the funds in DOD's appropriation accounts must be reduced or increased as the department spends money or receives collections that it is authorized to retain for its own use.

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become audit ready. The critical path milestones are considered priorities that DOD components still need to address. In addition, the department is still developing the details of its strategy for how to consolidate individual component financial statements into department-wide financial statements, which among other things, will need to address the elimination of intragovernmental transactions.

The effects of DOD's financial management problems extend beyond financial reporting. Long-standing control deficiencies adversely affect the economy, efficiency, and effectiveness of its operations. For example, as we have previously reported, DOD's financial management problems have contributed to (1) inconsistent and sometimes unreliable reports to Congress on estimated weapon system operating and support costs, limiting the visibility needed for effective oversight of the weapon system programs,<sup>21</sup> and (2) continuing reports of Antideficiency Act<sup>22</sup> violations—36 such violations reported from fiscal year 2011 through fiscal year 2015, totaling over \$1 billion—which emphasize DOD's inability to ensure that obligations and expenditures are properly recorded and do not exceed statutory levels of control.<sup>23</sup> Further, DOD faces challenges in its efforts to provide reasonable assurance of accountability for its property, plant, and equipment—knowing what it has, where it is located, what condition it is in, and what it cost.

With improvements to its financial management processes, DOD would be better able to provide its management and Congress with reliable, useful, and timely information on the results of its business operations. Effectively implementing needed improvements, however, continues to be a difficult task. While DOD has made efforts to improve its financial management, we have reported over the past few years significant internal control, financial management, and systems deficiencies, including the following:

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<sup>21</sup>GAO, *Defense Logistics: Improvements Needed to Enhance Oversight of Estimated Long-term Costs for Operating and Supporting Major Weapon Systems*, GAO-12-340 (Washington, D.C.: Feb. 2, 2012).

<sup>22</sup>Antideficiency Act, *codified, as amended*, at 31 U.S.C §§ 1341-1342, 1349-1352, 1511-1519.

<sup>23</sup>GAO, *DOD Financial Management: Actions Under Way Need to Be Successfully Completed to Address Long-standing Funds Control Weaknesses*, GAO-14-94 (Washington, D.C.: Apr. 29, 2014).

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- The Air Force and Navy need to establish sufficient controls for their military pay processes.<sup>24</sup>
  - The Defense Finance and Accounting Service did not fully implement the FIAR Guidance in the areas of planning, testing, and corrective actions for processing payments to contractors.<sup>25</sup>
  - Fundamental deficiencies in DOD funds control significantly impair its ability to properly use resources, produce reliable financial reports on the results of operations, and meet its audit readiness goals.<sup>26</sup>
  - The effective implementation of DOD's planned Enterprise Resource Planning (ERP) systems is considered by DOD to be critical to the success of all of its planned long-term financial improvement efforts.<sup>27</sup> However, as we have previously reported, DOD continues to encounter difficulties in implementing its planned ERP systems on schedule and within budget and experiences significant operational problems, such as deficiencies in data accuracy, inability to generate auditable financial reports, and the need for manual work-arounds.<sup>28</sup>

We have made numerous recommendations to DOD to address these financial management issues. We are encouraged by DOD's sustained

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<sup>24</sup>GAO, *DOD Financial Management: Improved Documentation Needed to Support the Air Force's Military Payroll and Meet Audit Readiness Goals*, GAO-16-68 (Washington, D.C.: Dec. 17, 2015), and *DOD Financial Management: Additional Efforts Needed to Improve Audit Readiness of Navy Military Pay and Other Related Activities*, GAO-15-658 (Washington, D.C.: Sept. 15, 2015).

<sup>25</sup>GAO, *DOD Financial Management: The Defense Finance and Accounting Service Needs to Fully Implement Financial Improvements for Contract Pay*, GAO-14-10 (Washington, D.C.: June 23, 2014).

<sup>26</sup>GAO-14-94.

<sup>27</sup>ERP systems are integrated, multifunction systems that perform business-related tasks, such as general ledger accounting and supply chain management. DOD considers their implementation essential to transforming its business operations and achieving its goal of audit readiness by fiscal year 2017.

<sup>28</sup>GAO, *DOD Business Systems Modernization: Additional Enhancements Are Needed for Army Business System Schedule and Cost Estimates to Fully Meet Best Practices*, GAO-14-470 (Washington, D.C.: Sept. 30, 2014); *DOD Business Systems Modernization: Air Force Business System Schedule and Cost Estimates*, GAO-14-152 (Washington, D.C.: Feb. 7, 2014); and *DOD Financial Management: Implementation Weaknesses in Army and Air Force Business Systems Could Jeopardize DOD's Auditability Goals*, GAO-12-134 (Washington, D.C.: Feb. 28, 2012).

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commitment to improving financial management and achieving audit readiness, but several DOD business operations, including financial management, remain on our list of high-risk programs.<sup>29</sup> DOD has financial management improvement efforts under way and is monitoring progress against milestones. However, we have found that DOD and its components have emphasized the assertion of audit readiness by milestone dates over the implementation of effective underlying processes, systems, and controls. While establishing milestones is important for measuring progress, DOD should not lose sight of the ultimate goal—implementing lasting financial management reform to help ensure that it has the systems, processes, and personnel to routinely generate reliable, useful, and timely financial management and other information critical to decision making and effective operations for achieving its missions. Continued congressional oversight of DOD's financial management improvement efforts will be critical to helping ensure that DOD achieves its financial management improvement and audit readiness goals. To assist Congress in its oversight efforts, we will continue to monitor DOD's progress and provide feedback on the status of its improvement efforts.

**Reconciling Intragovernmental Activity and Balances**

Despite significant progress over the past few years, the federal government continued to be unable to adequately account for and reconcile intragovernmental activity and balances between federal entities, which resulted in hundreds of billions of dollars in differences for fiscal year 2015. When preparing the governmentwide financial statements, intragovernmental activity and balances between federal entities should be in agreement and must be subtracted out, or eliminated, from the financial statements. If the two federal entities engaged in an intragovernmental transaction do not both record the same intragovernmental transaction in the same year and for the same amount, the intragovernmental transactions will not be in agreement, resulting in errors in the governmentwide financial statements. For example, the cost recorded by the federal entity buying a good or service should agree to the revenue recorded by the federal entity trading partner selling the good or service.

The Department of the Treasury (Treasury) has grouped intragovernmental activity and balances into the following five categories.

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<sup>29</sup>GAO, *High-Risk Series: An Update*, GAO-15-290 (Washington, D.C.: Feb. 11, 2015).

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- Fiduciary activities include investments in Treasury securities with the Bureau of the Fiscal Service (Fiscal Service), borrowing from the Fiscal Service and the Federal Financing Bank and related interest receivable and payable, interest expense and revenue, and federal loans receivable and payable.
  - Benefit activities include contributions by federal entities into employee benefit programs (retirement, life insurance, workers' compensation, and health benefits) administered by the Office of Personnel Management and the Department of Labor.
  - Buy/Sell activities between entities include buy and sell costs and revenues, accounts receivable and payable, and advances to and from others.
  - Transfers of funds include transfers payable and receivable, and transfers in and out without reimbursement.
  - General Fund of the U.S. Government (General Fund) transactions and balances include fund balance with Treasury, appropriations received and warrants, and custodial and non-entity collections.<sup>30</sup>

Treasury has various efforts under way to address this impediment, including the following key initiatives.

- Treasury implemented the Governmentwide Treasury Account Symbol Adjusted Trial Balance System in fiscal year 2014, which among other things, provided more complete financial data from entities that are intended to improve the analysis of intragovernmental differences.
- In fiscal year 2015, Treasury continued to actively work with significant federal entities to resolve intragovernmental differences

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<sup>30</sup>The General Fund is a component of Treasury's central accounting function. It is a stand-alone reporting entity that comprises the activities fundamental to funding the federal government (e.g., issued budget authority, cash activity, and debt financing activities).



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through its quarterly scorecard process.<sup>31</sup> This process highlights differences requiring the entities' attention, identifies differences that need to be resolved through a formal dispute resolution process as set out in the *Treasury Financial Manual*<sup>32</sup> and reinforces the entities' responsibilities to resolve intragovernmental differences.

- In the third quarter of fiscal year 2015, Treasury began implementing a new initiative to identify and monitor systemic root causes of intragovernmental differences.

As a result of these and other actions, a significant number of intragovernmental differences were identified and resolved. While progress was made, we continued to note that amounts reported by federal entity trading partners to Treasury were not in agreement by material amounts. Reasons for the differences cited by several CFOs included differing accounting methodologies, accounting errors, and timing differences. In addition, the auditor for DOD reported that DOD, which contributes significantly to the unreconciled amounts, could not accurately identify most of its intragovernmental transactions by customer and was unable to reconcile most intragovernmental transactions with trading partners, which resulted in adjustments that could not be fully supported.

Additionally, for fiscal year 2015, a significant portion of intragovernmental differences were related to unreconciled transactions between the General Fund and federal entity trading partners related to appropriations and other intragovernmental transactions, which amount to hundreds of billions of dollars. In fiscal year 2015, Treasury continued to make significant improvements to the processes used to identify and reconcile General Fund differences. For example, Treasury

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<sup>31</sup>The Office of Management and Budget (OMB) and Treasury identified 39 federal entities that were significant to the fiscal year 2015 governmentwide financial statements, including the 24 CFO Act agencies. For each quarter, Treasury produces a scorecard for each significant entity that reports various aspects of the entity's intragovernmental differences with its trading partners, including the composition of the differences by trading partner and category. Entities are expected to resolve, with their respective trading partners, the differences identified in their scorecards.

<sup>32</sup>When an entity and its respective trading partner cannot resolve an intragovernmental difference, the entity must request Treasury to resolve the dispute. Treasury will review the dispute and issue a decision on how to resolve the difference, which the entities must follow. See *Treasury Financial Manual*, vol. 1, part 2, ch. 4700, appx. 10, § 2.

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- established more specific guidance regarding General Fund-related activity and balances and issued this guidance for federal entities to follow in reporting their financial data;
  - began developing policies and procedures over accounting for and reporting all significant General Fund activity and balances;
  - began reconciling the activity and balances between the General Fund and federal entity trading partners; and
  - implemented certain reconciliations for subcategories relevant to the General Fund, such as debt financing activities.

However, the ability to effectively reconcile General Fund transactions will be hampered until General Fund-related activity and balances are properly accounted for, reported, and audited.

Over the years, we have made several recommendations to Treasury to address these issues. Treasury has taken or plans to take actions to address these recommendations.

#### Preparing the Governmentwide Financial Statements

Treasury, in coordination with the Office of Management and Budget (OMB), has implemented several corrective actions during the past few years related to the preparation of the governmentwide financial statements. Corrective actions included implementation of new systems to collect certain additional data from entities and to compile the governmentwide financial statements, and new or enhanced procedures to address certain internal control deficiencies detailed in our previously issued report.<sup>33</sup> However, the federal government continued to have inadequate systems, controls, and procedures to reasonably assure that the governmentwide financial statements are consistent with the underlying audited entity financial statements, properly balanced, and in accordance with U.S. GAAP. For example:

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<sup>33</sup>Most of the issues we identified in fiscal year 2015 existed in fiscal year 2014, and many have existed for a number of years. Most recently, in July 2015, we reported the issues we identified to Treasury and OMB and provided recommendations for corrective action. See GAO, *Management Report: Improvements Needed in Controls over the Processes Used to Prepare the U.S. Consolidated Financial Statements*, GAO-15-630 (Washington, D.C.: July 30, 2015). A detailed discussion of control deficiencies regarding the process for preparing the consolidated financial statements can be found on pp. 259 through 261 of the 2015 Financial Report.

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- Treasury was unable to properly balance the accrual-based financial statements. To make the fiscal years 2015 and 2014 governmentwide financial statements balance, Treasury recorded a net decrease of \$5.1 billion and a net increase of \$20.4 billion, respectively, to net operating cost on the Statements of Operations and Changes in Net Position, which were identified as "Unmatched transactions and balances."<sup>34</sup> Treasury recorded an additional net \$1.9 billion and \$1.7 billion of unmatched transactions in the Statement of Net Cost for fiscal years 2015 and 2014, respectively. The material weakness in the federal government's ability to account for and reconcile intragovernmental activity and balances, discussed above, significantly contributed to the unmatched transactions and balances and consequently impaired Treasury's ability to fully eliminate such intragovernmental activity and balances.
  - Treasury's ability to report certain financial information in accordance with U.S. GAAP continues to be impaired and will remain so until federal entities, such as DOD, can provide Treasury with complete and reliable information required to be reported in the governmentwide financial statements.

Over the years, we have made numerous recommendations to Treasury to address these issues, and Treasury has taken or plans to take actions to address these recommendations. In June 2014, we recommended that Treasury, working in coordination with OMB, include all key elements for preparing well-defined corrective action plans from the Chief Financial Officers Council's *Implementation Guide for OMB Circular A-123, Management's Responsibilities for Internal Control—Appendix A, Internal Control over Financial Reporting*, in Treasury's and OMB's corrective action plans. In fiscal year 2015, Treasury and OMB made significant progress with respect to their corrective action plans by developing a remediation plan that focuses on corrective actions to be taken over the next 3 years to address the material weaknesses in internal control. However, the plans continued to lack certain key elements, such as (1) sufficient information on how progress on interim actions would be monitored and (2) outcome measures for assessing the effectiveness of the corrective actions.

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<sup>34</sup>Although Treasury was unable to determine how much of the unmatched transactions and balances related to net operating cost, it reported this amount as a component of net operating cost in the consolidated financial statements.

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**Material Weaknesses  
Resulted in Ineffective  
Internal Control over  
Financial Reporting**

The material weaknesses discussed in our report resulted in ineffective internal control over financial reporting. In addition to the material weaknesses in internal control that contributed to our disclaimer on the financial statements, discussed above, there are three other material weaknesses that were identified during our audit of the fiscal year 2015 governmentwide financial statements. These additional material weaknesses consist of the federal government's inability to (1) determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to reduce them, (2) identify and resolve information security control deficiencies and manage information security risks on an ongoing basis, and (3) effectively manage its tax collection activities.<sup>35</sup>

**Improper Payments**

Improper payments are a significant and pervasive governmentwide issue.<sup>36</sup> Initial estimates of improper payments for certain programs were developed as part of the initial financial statement audits under GMRA, and we first reported that the federal government was unable to determine the full extent of improper payments in our report on the fiscal year 1997 governmentwide financial statements. Since fiscal year 2003—when certain agencies began reporting improper payments as required by the Improper Payments Information Act of 2002 (IPIA)—cumulative

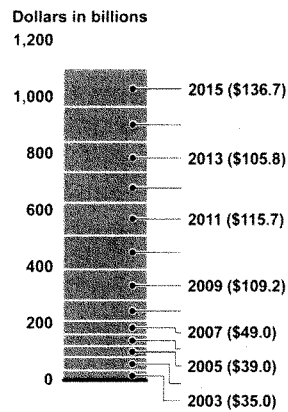
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<sup>35</sup>A detailed discussion of these material weaknesses, including the primary effects of the material weaknesses on the accrual-based financial statements and on the management of federal government operations, can be found on pp. 263 through 266 of the 2015 *Financial Report*.

<sup>36</sup>Under the Improper Payments Information Act of 2002 (IPIA), as amended, an improper payment is statutorily defined as any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements. It includes any payment to an ineligible recipient, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), and any payment that does not account for credit for applicable discounts. OMB guidance also instructs agencies to report as improper payments any payments for which insufficient or no documentation was found.

improper payment estimates have totaled over \$1 trillion,<sup>37</sup> as shown in figure 1.

**Figure 1: Cumulative Improper Payment Estimates for Fiscal Years 2003 through 2015**



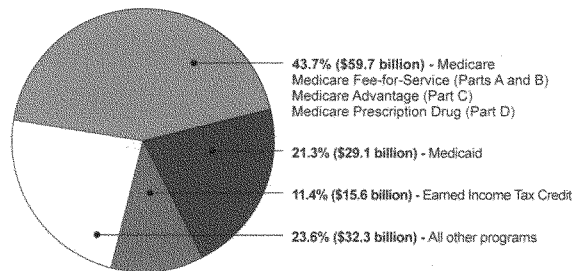
Source: GAO | GAO-16-541T

Note: Generally, the specific programs and total number of programs that constitute the governmentwide improper payment estimate vary from year to year. In earlier years, the number of programs included in the governmentwide estimate generally increased as programs reported improper payment estimates for the first time.

<sup>37</sup>IPIA—as amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA) and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA)—requires executive branch agencies to (1) review all programs and activities, (2) identify those that may be susceptible to significant improper payments, (3) estimate the annual amount of improper payments for those programs and activities identified as risk-susceptible, (4) implement actions to reduce improper payments and set reduction targets with respect to the risk-susceptible programs and activities, and (5) report on the results of addressing the foregoing requirements. IPIA, Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002), as amended by IPERA, Pub. L. No. 111-204, 124 Stat. 2224 (July 22, 2010), and IPERIA, Pub. L. No. 112-248, 126 Stat. 2390 (Jan. 10, 2013), and reprinted in 31 U.S.C. § 3321 note.

In fiscal year 2015, agencies reported improper payment estimates totaling \$136.7 billion, a significant increase—over \$12 billion, mainly due to an increased error rate in Medicaid—from the prior year's revised estimate of \$124.6 billion. The estimated governmentwide error rate increased from fiscal year 2014 to fiscal year 2015 (from 4.5 percent of program outlays to 4.8 percent).<sup>38</sup> The estimated improper payments for fiscal year 2015 were attributable to 121 programs spread among 22 agencies. While these 121 programs span various agencies across the federal government, improper payment estimates for Medicare, Medicaid, and the Earned Income Tax Credit accounted for more than 76 percent of the governmentwide estimate, as shown in figure 2.

**Figure 2: GovernmentWide Improper Payment Estimates by Program for Fiscal Year 2015**



Source: GAO analysis of agencies' data. | GAO-15-541T

We have identified various strategies and recommendations that could help to reduce improper payments in these key programs, including

<sup>38</sup>These estimates exclude DOD's Defense Finance and Accounting Service's Commercial Pay program because of concerns regarding the reliability of its improper payment estimate. When including the program, the governmentwide improper payment estimate was \$136.9 billion and the error rate was 4.4 percent for fiscal year 2015, up from \$124.6 billion and 4.0 percent in fiscal year 2014.

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requiring states to conduct audits of payments to and by Medicaid managed care organizations.<sup>39</sup>

The federal government has made progress in identifying programs that are susceptible to improper payments and including them in its estimate of governmentwide improper payments and recovering overpayments. However, further efforts are needed to ensure that all risk-susceptible programs are included, estimates are reliable, and improper payments are reduced. For example, three federal entities did not report fiscal year 2015 estimated improper payment amounts for five risk-susceptible programs, including the Department of Health and Human Services' Temporary Assistance for Needy Families. Further, various inspectors general reported deficiencies related to compliance with the criteria listed in the Improper Payments Elimination and Recovery Act of 2010 for fiscal year 2014 at their respective federal entities, including risk-susceptible programs that did not report improper payment estimates, estimation methodologies that may not produce reliable estimates, and risk assessments that may not accurately assess the risk of improper payment. Until the federal government has implemented effective processes to determine the full extent to which improper payments occur and has taken appropriate actions across entities and programs to effectively reduce improper payments, it will not have reasonable assurance that the use of federal funds is adequately safeguarded.

#### Information Security

GAO has reported information security as a high-risk area across government since February 1997. During our fiscal year 2015 audit, we found that serious and widespread information security control deficiencies continued to place

- federal assets at risk of inadvertent or deliberate misuse,
- financial information at risk of unauthorized modification or destruction,
- sensitive information at risk of inappropriate disclosure, and
- critical operations at risk of disruption.

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<sup>39</sup>GAO, *Fiscal Outlook: Addressing Improper Payments and the Tax Gap Would Improve the Government's Fiscal Position*, GAO-16-92T (Washington, D.C.: Oct. 1, 2015).

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Specifically, control deficiencies were identified related to (1) security management; (2) access to computer resources (data, equipment, and facilities); (3) changes to and configuration of information system resources; (4) segregation of incompatible duties; and (5) contingency planning. Such information security control deficiencies unnecessarily increase the risk that data recorded in or transmitted by federal financial management systems are not reliable and available.

Although significant challenges remain, the federal government has taken actions toward improving information security. For example, Congress passed and the President signed the Federal Information Security Modernization Act of 2014, and the Federal Chief Information Officer launched a 30-day Cybersecurity Sprint intended to improve the protection of federal information and systems. At the end of the Cybersecurity Sprint, according to OMB, federal agencies increased their use of strong authentication from 42 percent to 72 percent. Further, the administration has issued a cybersecurity strategy and implementation plan for federal civilian agencies to guide efforts to improve the security over their information and systems. It also plans to continue to oversee agency security efforts by monitoring the implementation of cybersecurity capabilities, such as strong authentication, continuous monitoring, anti-phishing and malware defense, and developing or monitoring performance-based metrics to measure their success.

However, until entities identify and resolve information security control deficiencies and manage information security risks on an ongoing basis, federal data and systems, including financial information, will remain at risk.

#### Tax Collection Activities

During fiscal year 2015, a material weakness continued to affect the federal government's ability to effectively manage its tax collection activities. Due to financial system limitations, as well as errors in taxpayers' accounts, the federal government's records did not always reflect the correct amount of taxes owed by the public to the federal government. Such errors may cause undue burden and frustration to taxpayers who either have already paid taxes owed or who owe significantly lower amounts.

Collectively, these deficiencies indicate that internal controls were not effective in (1) ensuring that reported amounts of taxes receivable and other tax assessments were accurate on an ongoing basis and could be relied upon by management as a tool to aid in making and supporting resource allocation decisions and (2) supporting timely and reliable



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financial statements, accompanying notes, and required supplementary information and other information without extensive supplemental procedures and adjustments.

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**Significant Uncertainties and a Material Weakness in Internal Control over Financial Reporting Resulted in a Disclaimer of Opinion on the Sustainability Financial Statements**

Significant uncertainties, which primarily related to the achievement of projected reductions in Medicare cost growth, affected the sustainability financial statements. In addition, the material weakness related to the (1) Reconciliations of Net Operating Cost and Unified Budget Deficit and (2) Statements of Changes in Cash Balance from Unified Budget and Other Activities, hampered the federal government's ability to demonstrate the reliability of historical budget information used for certain key inputs to the 2015 Statement of Long-Term Fiscal Projections.<sup>40</sup> As a result, these significant uncertainties and material weakness prevented us from expressing opinions on the 2015 Statement of Long-Term Fiscal Projections; the 2015, 2014, 2013, 2012, and 2011 Statements of Social Insurance;<sup>41</sup> and the 2015 and 2014 Statements of Changes in Social Insurance Amounts.<sup>42</sup> The sustainability financial statements present the present value of the federal government's estimated future receipts and future spending using a projection period sufficient to illustrate long-term sustainability.<sup>43</sup> The sustainability financial statements are intended to aid

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<sup>40</sup>As required by Statement of Federal Financial Accounting Standards No. 36, "Reporting Comprehensive Long-Term Fiscal Projections for the U.S. Government," as amended, the federal government presented a new basic financial statement, the Statement of Long-Term Fiscal Projections, for fiscal year 2015, along with the related notes, as part of the consolidated financial statements. The Statement of Long-Term Fiscal Projections presents, for all the activities of the federal government, the present value of projected receipts and noninterest spending under current policy without change, the relationship of these amounts to projected gross domestic product, and changes in the present value of projected receipts and noninterest spending from the prior year. The unaudited Statement of Long-Term Fiscal Projections for the fiscal year ended September 30, 2014, was presented for comparison purposes and was not subject to audit.

<sup>41</sup>Social insurance programs included in the Statement of Social Insurance are Social Security, Medicare, Railroad Retirement, and Black Lung.

<sup>42</sup>About \$27.9 trillion, or 67.3 percent, of the federal government's reported total present value of future expenditures in excess of future revenue presented in the 2015 Statement of Social Insurance relates to Medicare programs reported in the Department of Health and Human Services' 2015 Statement of Social Insurance, which received a disclaimer of opinion.

<sup>43</sup>The projection period used for the Social Security, Medicare, and Railroad Retirement social insurance programs is 75 years. For the Black Lung program, the projections are through September 30, 2040.

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users in assessing whether future resources will likely be sufficient to sustain public services and to meet obligations as they come due. The Statements of Social Insurance and Changes in Social Insurance Amounts are based on income and benefit formulas in current law and assume that scheduled benefits will continue after any related trust funds are exhausted.<sup>44</sup> The Statements of Long-Term Fiscal Projections are based on the continuation of current policy. The sustainability financial statements are not forecasts or predictions.

For 2015, these significant uncertainties primarily related to the following.

- Medicare projections in the 2015 Statement of Long-Term Fiscal Projections and the 2015 Statement of Social Insurance were based on benefit formulas under current law and included a significant reduction in Medicare payment rates for productivity improvements relating to most categories of Medicare providers,<sup>45</sup> based on full implementation of the provisions of the Patient Protection and Affordable Care Act, as amended (ACA),<sup>46</sup> and physician payment updates specified by the Medicare Access and CHIP Reauthorization Act of 2015 (MACRA).<sup>47</sup>
- Management has noted that actual future costs for Medicare are likely to exceed those shown by the current law projections presented in the 2015 Statement of Social Insurance due, for example, to the likelihood of modifications to the scheduled reductions in Medicare payment

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<sup>44</sup>The 2014 Statement of Social Insurance reflected a projected baseline that assumed that the physician payment rate reductions in current law would not occur and that physician payment rates would annually increase at a rate equal to the average sustainable growth rate (SGR) override that occurred over the 10-year period ending on March 31, 2015.

<sup>45</sup>These categories include, but are not limited to, inpatient/outpatient hospital services, skilled nursing facilities, home health care, ambulance, ambulatory surgical centers, durable medical equipment, and prosthetics.

<sup>46</sup>ACA, Pub. L. No. 111-148, 124 Stat. 119 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (Mar. 30, 2010). In this testimony, references to ACA include any amendments made by the Health Care and Education Reconciliation Act of 2010.

<sup>47</sup>MACRA, Pub. L. No. 114-10, title I, § 101, 129 Stat. 87, 89 (Apr. 16, 2015). MACRA included many provisions that affect Medicare, including the repeal of the SGR formula for calculating annual updates to Medicare reimbursement payment rates to physicians and certain nonphysician medical providers and established an alternative set of annual updates.

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rates for productivity adjustments relating to most categories of Medicare providers and to the specified physician payment updates. The extent to which actual future costs exceed the current law projected amounts due to changes to the scheduled reductions in Medicare payment rates for productivity adjustments and to the specified physician payment updates depends on both the specific changes that might be legislated and whether such legislation would include further provisions to help offset such costs. Consequently, there are significant uncertainties concerning the achievement of these projected reductions in Medicare payment rates.

- Management has developed an illustrative alternative projection intended to provide additional context regarding the long-term sustainability of the Medicare program and to illustrate the uncertainties in the Statement of Social Insurance projections. The present value of future estimated expenditures in excess of future estimated revenue for Medicare, included in the illustrative alternative projection, exceeds the \$27.9 trillion estimate in the 2015 Statement of Social Insurance by \$8.9 trillion.
- Management noted that these significant uncertainties about projected reductions in health care cost growth also affect the projected Medicare and Medicaid costs reported in the 2015 Statement of Long-Term Fiscal Projections.

Projections of Medicare costs are sensitive to assumptions about future decisions by policymakers and about the behavioral responses of consumers, employers, and health care providers as policy, incentives, and the health care sector change over time. Such secondary impacts are not fully reflected in the sustainability financial statements but could be expected to influence the excess cost growth rate used in the projections.<sup>48</sup> Key drivers of uncertainty about the excess cost growth rate include the future development and deployment of medical technology, the evolution of personal income, and the cost and availability of insurance, as well as federal policy changes, such as the implementation of ACA.

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<sup>48</sup>The excess cost growth rate is the increase in health care spending per person relative to the growth of gross domestic product per person after removing the effects of demographic changes on health care spending.

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**The *Financial Report* Presents Important Information on Accrual Costs Incurred by the Federal Government and Highlights Certain Financial Risks**

Because the federal government's and individual agencies' financial statements are presented on an accrual basis, they include information on the federal government's liabilities and highlight certain financial risks that are not included in the generally cash-based budget. As reported in the *2015 Financial Report*, the federal government's reported "bottom line" accrual net operating cost for fiscal year 2015 of \$520 billion was \$81 billion higher than the reported budget deficit of \$440 billion. The excess of the accrual net operating cost over the budget deficit is primarily due to accrued costs (incurred but not necessarily paid) associated with increases in estimated federal employee and veteran benefits liabilities and certain other liabilities that are included in net operating cost, but not the budget deficit.

Examples of liabilities and related costs that are recognized in the *Financial Report* as of September 30, 2015, but are not recognized in the budget include the following:

- Federal employee and veteran benefits payable for benefits earned but not yet paid of \$6.7 trillion,
- Environmental and disposal liabilities for cleaning up environmental contamination of \$412 billion, and
- Insurance and guarantee program liabilities for estimated unpaid insurance and guarantee program claims of \$178 billion.

Additionally, the *2015 Financial Report* and individual agency financial statements provide information related to risks that could affect the federal government's financial condition in the future, including the following.

- The Pension Benefit Guaranty Corporation's (PBGC) financial future is uncertain because of long-term challenges related to PBGC's governance and funding structure. PBGC's liabilities exceeded its assets by over \$76 billion as of September 30, 2015—an increase of over \$14 billion from the end of fiscal year 2014. PBGC reported that it is subject to further losses if plan terminations that are considered reasonably possible occur.
- In 2008, during the financial crisis, the federal government placed the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) under conservatorship and entered into preferred stock purchase agreements with these government-sponsored enterprises (GSE) to

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help ensure their financial stability. The agreements with the GSEs could affect the federal government's financial position. As of September 30, 2015, the federal government continued to report about \$106 billion of investments in the GSEs, which is net of about \$88 billion in valuation losses. Cash dividends paid by the GSEs to Treasury under the agreements totaled \$20.4 billion and \$72.5 billion during fiscal years 2015 and 2014, respectively. Although Treasury does not believe that any further draws by the GSEs are probable, the reported maximum remaining contractual commitment to the GSEs, if needed, is \$258.1 billion. Importantly, the ultimate role of the GSEs in the mortgage market could affect the financial condition of the Federal Housing Administration, which in the past expanded its lending role in distressed housing and mortgage markets.

- The U.S. Postal Service (USPS) continues to be in a serious financial crisis as it has reached its borrowing limit of \$15 billion and finished fiscal year 2015 with a reported net loss of \$5.1 billion.

Every 2 years, GAO provides Congress with an update on its High Risk Series, which highlights federal entities and program areas that are at high risk due to their vulnerabilities to fraud, waste, abuse, and mismanagement or are most in need of broad reform. We issued our most recently updated High Risk Series on February 11, 2015.<sup>49</sup> GAO's High Risk Series includes most of the above-noted issues, such as DOD financial management, government information security, USPS's business model, the PBGC insurance programs, and the financial regulatory system for housing finance. Another area included in the High Risk Series that could affect the federal government's financial condition in the future is the Internal Revenue Service's (IRS) enforcement of tax laws, including reducing the net tax gap—the difference between taxes owed and taxes paid—which was last estimated to be \$385 billion. Unaudited information on the tax gap is also reported in the *Financial Report*.

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<sup>49</sup>GAO-15-290.

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Even modest reductions of the net tax gap would result in billions of dollars in additional revenue collected each year.<sup>50</sup> We have made various recommendations to IRS on reducing the tax gap that remain open, including using return on investment data to reallocate its enforcement resources and potentially increase revenues and making improvements to telephone and online services to help IRS deliver high-quality services to taxpayers who wish to comply with tax laws but do not understand their obligations.<sup>51</sup>

Other strategies we have suggested to address the tax gap would require legislative actions, such as requiring additional taxpayers to electronically file tax and information returns, which could help IRS improve compliance in a resource-efficient way. We have also suggested that Congress consider granting IRS the authority to regulate paid tax preparers. In a limited study, we found that preparers made significant errors.<sup>52</sup> Because paid tax preparers account for almost 60 percent of all tax returns filed, they have an enormous impact on IRS's ability to administer tax laws effectively. Finally, IRS has the authority to correct calculation errors and check for other obvious noncompliance, such as claims above income and credit limits. Expanding such authority—which we have suggested Congress consider with appropriate safeguards—could help IRS correct additional errors and avoid burdensome audits and taxpayer penalties.<sup>53</sup>

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<sup>50</sup>IRS last estimated the tax gap in 2012 for tax year 2006. IRS estimated the gross tax gap to be \$450 billion, of which it would eventually recover about \$65 billion through late payments and enforcement actions, leaving an annual net tax gap of about \$385 billion. According to an IRS official, the agency plans to release an updated tax gap estimate in 2016, which will be based on tax years 2008, 2009, and 2010.

<sup>51</sup>GAO-16-92T, and GAO, *Tax Gap: IRS Could Significantly Increase Revenues by Better Targeting Enforcement Resources*, GAO-13-151 (Washington, D.C.: Dec. 5, 2012).

<sup>52</sup>GAO, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors*, GAO-14-467T (Washington, D.C.: Apr. 8, 2014).

<sup>53</sup>GAO, *Recovery Act: IRS Quickly Implemented Tax Provisions, but Reporting and Enforcement Improvements Are Needed*, GAO-10-349 (Washington, D.C.: Feb. 10, 2010). We recently recommended that IRS assess whether data received from the health insurance marketplaces are sufficiently complete and accurate to be used to correct claims for the premium tax credit on returns, and if the assessment determines that such corrections would be effective, seek legislative "correctible error" authority for this specific purpose. GAO, *Patient Protection and Affordable Care Act: IRS Needs to Strengthen Oversight of Tax Provisions for Individuals*, GAO-15-540 (Washington, D.C.: July 29, 2015).

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## Long-Term Fiscal Challenges

The comprehensive long-term fiscal projections for the government included in the *2015 Financial Report* provide a much needed perspective on the federal government's long-term fiscal position and outlook. Although the timing and size of the increase in debt as a share of gross domestic product (GDP) varies depending on the assumptions used, both the long-term fiscal projections for the government included in the *2015 Financial Report* and GAO's own recent long-term fiscal simulations show that, absent policy changes, the federal government continues to face an unsustainable long-term fiscal path.<sup>54</sup> The projections included in the *2015 Financial Report* and our simulations both underscore the need to take action soon to address the long-term path to avoid larger policy changes in the future that could be disruptive to individuals and the economy, while also taking into account concerns about near-term economic growth.

In the near term, the projections in the *2015 Financial Report* show the primary deficit continuing to decline from the recent historic highs. However, these projections do not reflect recent legislation enacted subsequent to September 30, 2015, which, in order to achieve certain national priorities and goals, causes deficits to increase in the near term.<sup>55</sup> Both the projections in the *2015 Financial Report* and our long-term simulations follow the spending limits enacted in the Balanced Budget

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<sup>54</sup>We prepare long-term federal fiscal simulations, using different sets of assumptions. See GAO, *Fiscal Outlook: Federal Fiscal Outlook* (2016), (Washington, D.C.: 2016), accessed April 1, 2016, [http://www.gao.gov/fiscal\\_outlook/federal\\_fiscal\\_outlook/overview](http://www.gao.gov/fiscal_outlook/federal_fiscal_outlook/overview).

<sup>55</sup>The 2015 Statement of Long-Term Fiscal Projections is based on current policy as of September 30, 2015. This is prior to the enactment of the Bipartisan Budget Act of 2015 and the Consolidated Appropriations Act, 2016; therefore, the projections do not reflect the effects of these two statutes. Management notes that neither statute is expected to have a material effect on the long-term fiscal projections in its report.

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and Emergency Deficit Control Act of 1985 (BBEDCA), as amended.<sup>56</sup>

Under these limits, discretionary spending will continue to decline as a share of the economy and within the next 5 years will be lower as a share of GDP than any level seen in the last 50 years. At the same time, the projections in the *2015 Financial Report* show revenues rising in the near term as the economy continues to recover. Our long-term simulations show revenues rising in some years and declining in others in the near term.

Over the long term, at the federal level, the imbalance between spending and revenue that is built into current law and policy is projected to lead to continued growth of debt held by the public as a share of GDP. This situation—in which debt grows faster than GDP—means the current federal fiscal path is unsustainable. Today, debt held by the public as a share of GDP remains well above the post-war historical average of 43 percent since 1946. At the end of fiscal year 2015, it reached about 74 percent of GDP—the second highest (after fiscal year 2014, when it was slightly higher) since 1950.

Under our long-term simulations, debt held by the public as a share of GDP will surpass its historical high (106 percent in 1946) within 15 to 25 years (see fig. 3). By 2089, the last year of GAO's 75-year projection period, debt held by the public as a share of GDP reaches 314 percent in

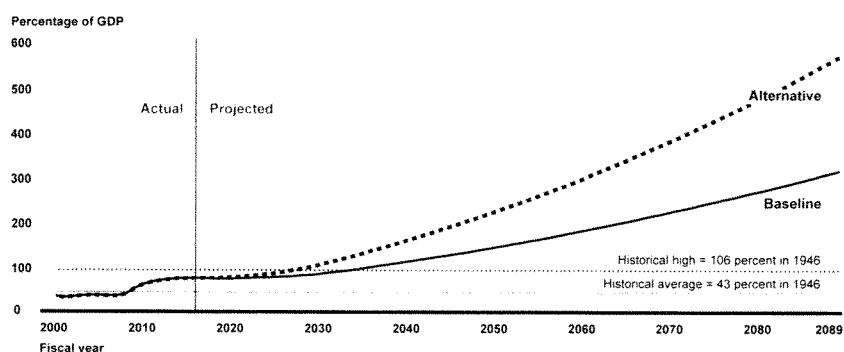
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<sup>56</sup>The Budget Control Act of 2011 (BCA) amended BBEDCA, imposing discretionary spending limits for fiscal years 2012 through 2021 to reduce projected spending by about \$1 trillion. Pub. L. No. 112-25, 125 Stat. 240 (Aug. 2, 2011). BCA also established the Joint Select Committee on Deficit Reduction (Joint Committee), which was tasked with proposing legislation to reduce the deficit by at least an additional \$1.2 trillion through fiscal year 2021. The Joint Committee did not report a proposal, and Congress and the President did not enact legislation. This triggered the sequestration process in section 251A of BBEDCA. Section 251A, as amended by BCA, required (1) a sequestration for fiscal year 2013 and (2) annual downward adjustments to discretionary spending limits and sequestration of direct spending from fiscal years 2014 through 2021. BBEDCA has been amended several times since August 2011, most recently by the Bipartisan Budget Act of 2015 (BBA), which increased discretionary spending limits for fiscal years 2016 and 2017. BBA also extended the sequestration of direct spending through fiscal year 2025 and made other changes to direct spending and revenue. Pub. L. No. 114-74, §§ 101, 102, 129 Stat. 584, 585-87 (Nov. 2, 2015). Our long-term simulations reflect the effects of BBA.



our baseline extended simulation or 568 percent in our alternative simulation.<sup>57</sup>

**Figure 3: Debt Held by the Public under GAO's Two Policy Simulations**



Source: GAO. GAO-16-541T

Note: Data are from GAO's 2016 simulations.

The federal government will not be able to sustain these budget paths over the long term. Debt at these high levels could limit the federal government's flexibility to address emerging issues and unforeseen challenges, such as another economic downturn or large-scale disaster. Our past work has identified a variety of fiscal exposures—

<sup>57</sup>We run two long-term simulations—the baseline extended and alternative. The baseline extended simulation begins with a baseline using Congressional Budget Office estimates and generally assumes current law continues into the future, such as the expiration of tax credits as scheduled. The alternative simulation changes some of the baseline assumptions to reflect historical trends rather than current law. For example, tax provisions that are scheduled to expire are extended and discretionary spending follows the caps established in the Balanced Budget and Emergency Deficit Control Act of 1985, as amended, but not the lower caps triggered by the automatic enforcement procedures. For more information on our simulations, see GAO, *Fiscal Outlook: Federal Fiscal Outlook* (2016), accessed April 1, 2016, [http://www.gao.gov/fiscal\\_outlook/federal\\_fiscal\\_outlook/overview](http://www.gao.gov/fiscal_outlook/federal_fiscal_outlook/overview).

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responsibilities, programs, and activities that explicitly or implicitly expose the federal government to future spending.<sup>58</sup> Fiscal exposures vary widely as to source, extent of the government's legal commitment, and magnitude. Examples are responses to natural disasters, pension guarantees, financial crises, and ensuring care for veterans. Over the past decade, some fiscal exposures have grown due to events and trends and the government's response to them. Increased attention to these fiscal exposures will be important for understanding risks to the federal fiscal outlook and enhancing oversight of federal resources.

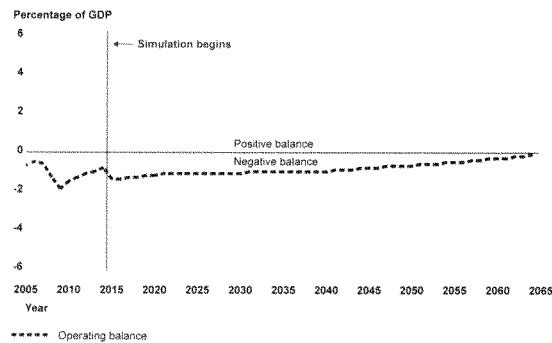
Our simulations show that all levels of government face long-term fiscal challenges, which could affect future federal funding of intergovernmental programs, as well as the potential capacity of state and local governments to help fund and implement these programs. As shown in figure 4, our simulations suggest that the state and local government sector could continue to face a gap between revenue and spending during the next 50 years, and that state and local governments would need to make substantial policy changes to avoid these fiscal imbalances in the future.<sup>59</sup> The simulation assumes that the tax structure is unchanged in the future and that the provision of real government services per capita remains relatively constant.

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<sup>58</sup>GAO, *Fiscal Outlook: Federal Fiscal Outlook* (2016), accessed April 1, 2016, [http://www.gao.gov/fiscal\\_outlook/federal\\_fiscal\\_outlook/overview](http://www.gao.gov/fiscal_outlook/federal_fiscal_outlook/overview) and *Fiscal Exposures: Improving Cost Recognition in the Federal Budget*, GAO-14-28 (Washington, D.C.: Oct. 29, 2013).

<sup>59</sup>GAO, *State and Local Government's Fiscal Outlook: 2015 Update*, GAO-16-260SP (Washington, D.C.: Dec. 16, 2015). See also, GAO, *Fiscal Outlook: State and Local Fiscal Model* (2015), accessed April 1, 2016, [http://www.gao.gov/fiscal\\_outlook/state\\_local\\_fiscal\\_model/overview](http://www.gao.gov/fiscal_outlook/state_local_fiscal_model/overview).

**Figure 4: State and Local Simulated Operating Balance Measure, as a Percentage of Gross Domestic Product (GDP)**



Sources: GAO calculations using Bureau of Economic Analysis data and GAO simulations, updated December 2015. | GAO-16-5417

Notes: The simulated operating balance is a measure of the sector's ability to cover its current expenditures out of current receipts. The simulated operating balance measure is all receipts, excluding funds used for long-term investments, minus current expenditures. See GAO-16-260SP for details on how we developed this measure.

The interconnectedness that defines intergovernmental programs requires that officials at all levels of government remain aware of and ready to respond to fiscal pressures. This interconnectedness is something that must be kept in mind as decision makers seek to address the federal fiscal challenge.

## Debt Limit

As discussed in our report on the *Financial Report*, the debt limit does not restrict Congress's ability to enact spending and revenue legislation that affects the level of federal debt or otherwise constrain fiscal policy; it restricts Treasury's authority to borrow to finance the decisions already enacted by Congress and the President.<sup>60</sup> The United States benefits

<sup>60</sup>GAO, *Debt Limit: Analysis of 2011-2012 Actions Taken and Effect of Delayed Increase on Borrowing Costs*, GAO-12-701 (Washington, D.C.: July 23, 2012), and *Debt Limit: Delays Create Debt Management Challenges and Increase Uncertainty in the Treasury Market*, GAO-11-203 (Washington, D.C.: Feb. 22, 2011).

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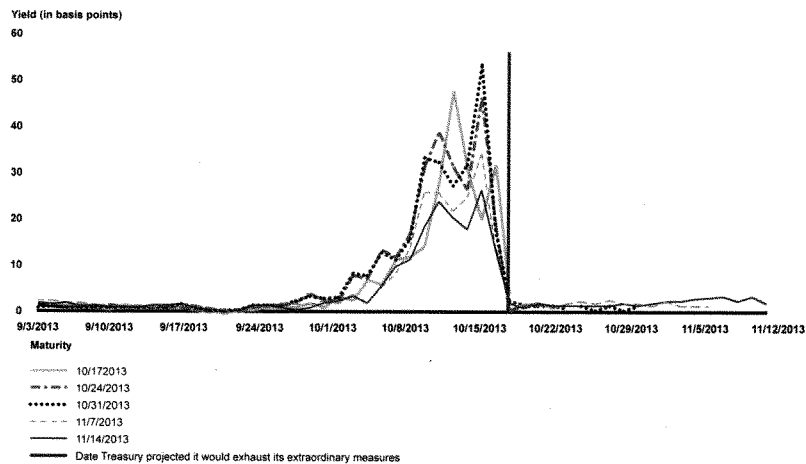
from the confidence investors have that debt backed by the full faith and credit of the United States will be honored. Because Treasury securities are viewed as one of the safest assets in the world, they are broadly held by individuals—often in pension funds or mutual funds—and by institutions and central banks for use in everyday transactions. In many ways, Treasury securities are the underpinning of the world financial system.

In our July 2015 report on the debt limit, we found that during the 2013 debt limit impasse, investors reported taking the unprecedented action of systematically avoiding certain Treasury securities—those that matured around the dates when Treasury projected it would exhaust the extraordinary measures that it uses to manage federal debt when it is at the limit.<sup>61</sup> For the affected Treasury securities, these actions resulted in both a dramatic increase in rates and a decline in liquidity in the secondary market where securities are traded among investors. In 2013, secondary market yields on Treasury bills maturing in late October through mid-November rose from about 1 basis point (or one-one hundredth of a percent) in mid-September to over 50 basis points prior to the resolution of the impasse on October 17 (see fig. 5). In addition, there were also unusually low levels of demand at the relevant auctions and additional borrowing costs to Treasury. Treasury securities are one of the lowest cost and widely used forms of collateral for financial transactions, and because of this, disruptions to the Treasury market from the 2013 debt limit impasse extended into other markets, such as short-term financing.

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<sup>61</sup>GAO, *Debt Limit: Market Response to Recent Impasses Underscores Need to Consider Alternative Approaches*, GAO-15-476 (Washington, D.C.: July 9, 2015).

Figure 5: Secondary Market Yields on Treasury Bills Maturing in Late October through Mid-November 2013 (in Basis Points)



Source: GAO analysis of Bloomberg data. | GAO-16-541T

In July 2015, we reported that investors told us that they were now prepared to take similar steps to systematically avoid certain Treasury securities during future debt limit impasses. Market participants with whom we spoke said market reaction to future impasses could be more severe, in part because of changes in market practices since the financial crisis and in part because of contingency plans that many investors now have in place. Industry groups emphasized that even a temporary delay in payment could undermine confidence in the full faith and credit of the United States and therefore cause significant damage to markets for Treasury securities and other assets. This would affect not only institutions, but also individuals.

While increased rates on Treasury securities in the secondary market affect the amount of return on investment for private investors, changes in the rates paid at Treasury auctions affect the amount that Treasury—and

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ultimately the American taxpayer—pays in interest on federal debt. Our analysis indicated that the additional borrowing costs that Treasury incurred rose rapidly in the final weeks and days leading up to the October 2013 deadline when Treasury projected it would exhaust its extraordinary measures. We estimated the total increased borrowing costs incurred through September 30, 2014, on securities issued by Treasury during the 2013 debt limit impasse. These estimates ranged from roughly \$38 million to more than \$70 million, depending on the specifications used.

To avoid uncertainty and the disruption to the Treasury market that it creates, as well as to help inform the fiscal policy debate in a timely way, we have suggested that Congress should consider ways to better link decisions about the debt limit with decisions about spending and revenue at the time those decisions are made.<sup>62</sup> In our July 2015 report, we discussed several potential approaches to delegating borrowing authority that Congress could consider that would both achieve this link and minimize disruptions to the market.<sup>63</sup> All of the options also maintain congressional control and oversight of federal borrowing. These approaches are as follows:

- **Link action on the debt limit to the budget resolution:** This is a variation of a previously used approach under which legislation raising the debt limit to the level envisioned in the Congressional Budget Resolution would be spun off and either be deemed to have passed or be voted on immediately thereafter.
- **Provide the administration with the authority to increase the debt limit, subject to a congressional motion of disapproval:** This is a variation of an approach contained in the Budget Control Act of 2011. Congress would give the administration the authority to propose a change in the debt limit, which would take effect absent enactment of a joint resolution of disapproval within a specified time frame.
- **Delegate broad authority to the administration to borrow as necessary to fund enacted laws:** This is an approach used in some other countries: delegate to the administration the authority to borrow

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<sup>62</sup>GAO-12-701 and GAO-11-203.

<sup>63</sup>GAO-15-476.

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such sums as necessary to fund implementation of the laws duly enacted by Congress and the President. Since laws that affect federal spending and revenue that create the need for debt already require adoption by Congress, Congress would still maintain control over the amount of federal borrowing.

To further assist with congressional consideration, our July 2015 report identified key design issues to consider for each option.<sup>64</sup>

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In closing, while progress has been made in addressing federal financial management challenges, much work remains given the federal government's long-term fiscal path and the need for Congress, the administration, and federal managers to have more reliable, useful, and timely financial and performance information to effectively meet these challenges, to make sound decisions, and to operate as efficiently and effectively as possible. The Financial Report, including sustainability reporting, and the Budget are both critical to understanding the fiscal and financial condition of the federal government. As the Budget Committee, you know that the federal budget serves as the primary financial plan of the government and plays a critical role in the decision-making process. Policymakers, managers, and the American people rely on it to frame their understanding of significant choices about the role of the government and to provide them with information to make decisions about individual programs and overall fiscal policy. The information in the financial statements can help further inform budget deliberations. Agencies must continue to strive toward routinely producing reliable, useful, and timely information to help guide decision makers on a day-to-day basis. Federal entities' improvement of financial management practices and systems will be essential to achieving this goal for their agencies and the federal government as a whole.

Meaningful improvement in financial and performance management will not occur without sustained commitment by executive branch leaders and managers and continued oversight by Congress. The single most important element of successful financial and performance management improvement efforts is the demonstrated commitment and personal

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<sup>64</sup>For additional information on the federal government's financial management challenges and long-term fiscal path, see Related Products in app. II.

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involvement of top leaders. Demonstrating leadership support for accountability and improvement by promoting capacity building and use of evidence is also essential to facilitating program evaluation use in agency program management and policy making. Similarly, Congress can play a decisive role in fostering results-oriented cultures in the federal government by using information on agency goals and asking for and using financial and performance information as it carries out its various legislative responsibilities.

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Chairman Enzi, Ranking Member Sanders, and Members of the Committee, this concludes my prepared statement. I would be pleased to respond to questions.

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## Appendix I: Chief Financial Officers (CFO) Act Agencies: Fiscal Year 2015 Audit Results and Principal Auditors

CFO Act agencies	Opinion expressed by agency auditor	Agency auditor-reported material weaknesses or noncompliances <sup>a</sup>	Principal auditor
Agency for International Development	Unmodified	√	Office of Inspector General (OIG)
Department of Agriculture	Disclaimer	√	OIG
Department of Commerce	Unmodified		KPMG LLP
Department of Defense	Disclaimer	√	OIG
Department of Education	Unmodified	√	CliftonLarsonAllen LLP
Department of Energy	Unmodified	√	KPMG LLP
Environmental Protection Agency	Unmodified	√	OIG
General Services Administration	Unmodified		KPMG LLP
Department of Health and Human Services	b	√	Ernst & Young LLP
Department of Homeland Security	Unmodified	√	KPMG LLP
Department of Housing and Urban Development	Disclaimer	√	OIG
Department of the Interior	Unmodified	√	KPMG LLP
Department of Justice	Unmodified		KPMG LLP
Department of Labor	Unmodified	√	KPMG LLP
National Aeronautics and Space Administration	Unmodified	√	CliftonLarsonAllen LLP
National Science Foundation	Unmodified	√	CliftonLarsonAllen LLP
Nuclear Regulatory Commission	Unmodified		CliftonLarsonAllen LLP
Office of Personnel Management	Unmodified	√	KPMG LLP
Small Business Administration	Unmodified	√	KPMG LLP
Social Security Administration	Unmodified		Grant Thornton LLP
Department of State	Unmodified	√	Kearney & Company
Department of Transportation	Unmodified	√	KPMG LLP
Department of the Treasury	Unmodified	√	KPMG LLP
Department of Veterans Affairs	Unmodified	√	CliftonLarsonAllen LLP

Source: GAO. | GAO-15-541T

<sup>a</sup>These include reported noncompliance with laws and regulations, substantial noncompliance with one or more of the Federal Financial Management Improvement Act requirements, or both.

<sup>b</sup>The auditors expressed an unmodified opinion on the Department of Health and Human Services' fiscal year 2015 accrual-based financial statements, but were unable to express opinions on the department's 2015 Statement of Social Insurance and 2015 Statement of Changes in Social Insurance Amounts.

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## Appendix II: Related Products

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*Financial Audit: U.S. Government's Fiscal Years 2015 and 2014 Consolidated Financial Statements*

<http://www.gao.gov/products/GAO-16-357R>

GAO-16-357R: Published Feb. 25, 2016. Publicly Released: Feb. 25, 2016.

*Management Report: Improvements Needed in Controls over the Processes Used to Prepare the U.S. Consolidated Financial Statements*

<http://www.gao.gov/products/GAO-15-630>

GAO-15-630: Published Jul. 30, 2015. Publicly Released: Jul. 30, 2015.

*Debt Limit: Market Response to Recent Impasses Underscores Need to Consider Alternative Approaches*

<http://www.gao.gov/products/GAO-15-476>

GAO-15-476: Published: Jul. 9, 2015. Publicly Released: July. 9, 2015.

*Capital Financing: Alternative Approaches to Budgeting for Federal Real Property*

<http://www.gao.gov/products/GAO-14-239>

GAO-14-239: Published: Mar. 12, 2014. Publicly Released: Mar. 12, 2014.

*Understanding the Primary Components of the Annual Financial Report of the United States Government*

<http://www.gao.gov/products/GAO-09-946SP>

GAO-09-946SP: Published: Sept. 25, 2009. Publicly Released: Sept. 25, 2009.

*A Glossary of Terms Used in the Federal Budget Process*

<http://www.gao.gov/products/GAO-05-734SP>

GAO-05-734SP: Published: Sept. 1, 2005. Publicly Released: Sept. 1, 2005.

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**Appendix II: Related Products**

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***Fiscal Outlook & the Debt***

[http://www.gao.gov/fiscal\\_outlook/overview](http://www.gao.gov/fiscal_outlook/overview)

contains tabs on

- *Understanding the Federal Debt*  
[http://www.gao.gov/fiscal\\_outlook/understanding\\_federal\\_debt/overview](http://www.gao.gov/fiscal_outlook/understanding_federal_debt/overview)
- *Measuring the Federal Deficit*  
[http://www.gao.gov/fiscal\\_outlook/measuring\\_the\\_federal\\_deficit/overview](http://www.gao.gov/fiscal_outlook/measuring_the_federal_deficit/overview)
- *The State & Local Outlook*  
[http://www.gao.gov/fiscal\\_outlook/state\\_local\\_fiscal\\_model/overview](http://www.gao.gov/fiscal_outlook/state_local_fiscal_model/overview)
- *The Federal Fiscal Outlook*  
[http://www.gao.gov/fiscal\\_outlook/federal\\_fiscal\\_outlook/overview](http://www.gao.gov/fiscal_outlook/federal_fiscal_outlook/overview)

***Duplication and Cost Savings: Annual Reports and Action Tracker***

<http://www.gao.gov/duplication/overview>



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Chairman ENZI. Thank you for your testimony and for the documents that you provide during the year and now. And this is really an exciting hearing for an accountant. [Laughter.]

But we are going to have a little bit of an interruption—well, we are going to try to not have an interruption. At 11 o'clock there is a vote, so I am going to turn over the chair to Senator Johnson, who is the other accountant here, and he can ask his questions during the time that I go vote, and then I can relieve him while he votes. And as such, I will pass on my questions for the moment and allow the Ranking Member to go, and then Senator Johnson will follow him as the Chair while I vote.

Senator WARNER. Well, thank you, Mr. Chairman.

I want to get right into the nitty-gritty, and, again, Gene, thank you for your good work. I want to get a couple questions in on the DATA Act. For my colleagues who have not followed all that closely, the DATA Act was an effort to try to make sure that we had at least common definitions. You cannot find any kind of level of transparency if you do not at least have common definitions about what spends are and what transfers are and what is a cost and what is not a cost.

In your January report, you highlighted the need for Treasury and OMB to issue more complete and timely guidance to agencies. I want to make sure that the agencies are moving forward on this. Later today, I will be sending a letter to the heads of 37 agencies and departments who submitted DATA Act implementation plans to OMB last fall. My goal is to gently noodge them—or maybe not so gently noodge them—to make sure that they understand the importance and benefit of financial transparency and to make sure they prioritize the implementation of this law. It will require additional resources. Again, I think it is so critical that Congress funds the \$50 million that is going to be required to set up these new systems. And, again, I would remind my colleagues this was very bipartisan. Senator Portman and Congressman Issa were leaders as well on it.

Your report said that the DATA Act holds “great promise to improve Government financial management.” But in January, you said there was a lack of clear guidance from both Treasury and OMB on how agencies should report their standardized spending data under the DATA Act, and that could hurt agencies’ efforts to prepare for the full 2017 implementation.

Do feel like that report has spurred change? And how do you evaluate the status of implementation of this law?

Mr. DODARO. I believe that OMB and Treasury understand our point, but they have yet to issue the guidance that we have called for, in two respects:

One, as you mentioned, concerns the reporting guidance on how to report on the data standards. They have issued the data standards, they are out there. But more is needed regarding how agencies should report. Based on our experience in the Recovery Act, particular areas of reporting such as place of where the activity takes place, the award descriptions, exactly what was done—those things need additional guidance. Otherwise, you will get information that will not be helpful.

Secondly, the DATA Act, as you know, requires machine-readable, downloadable information, and you need to have technical standards to be able to report that. Those technical standards in the Schema have not been set yet. Both of these issues are giving agencies pause, and they will not be able to finalize their implementation plans. So I am hopeful that the guidance on both these issues will be issued as soon as possible and be stabilized. The concern I have is that they not continue to revise things; otherwise, the agencies will have a legitimate excuse not to be fully prepared to meet the schedule under the DATA Act.

Senator WARNER. So appropriate guidance, would you say that falls into your category as we look at the litany of challenges between now and May of 2017 for full implementation?

Mr. DODARO. Yes, there—

Senator WARNER. Do you want to list some of the other issues?

Mr. DODARO. Yes. First, there is appropriate guidance. There is also a need to have a governance structure for the full cycle of setting and revising data standards. They have set up a temporary structure. They issued the initial data standards. But I am very concerned about the fact that the act will be implemented in the transition of two administrations, and there are huge opportunities here for loss of momentum, lack of clarity and guidance, and so I am encouraging them to put a permanent data governance structure in place.

Third, I am disappointed that they continue to defer the definition of “program” and to come up with a program inventory of the Federal Government. That has been continually deferred since the Government Performance and Results Modernization Act. They have said that they will do it under the DATA Act now. They have said it will be several years after the DATA Act is implemented before that would be in place. That is going to inhibit the ability to link the spending to programs which is one of the major objectives of the act. So I am very concerned about that deferral.

Senator WARNER. And would you also agree, when you pointed out in your report close to \$1 trillion—that was more on improper payments.

Mr. DODARO. Right.

Senator WARNER. On the improper—

Mr. DODARO. Well, but this would help on improper payments.

Senator WARNER. This would help on improper payments and intergovernmental transfers.

Mr. DODARO. It provides more transparency and more accountability, and you could do better tracking. The other—

Senator WARNER. Let me just get—because my time is about run out. On improper payments, any comments you want to make about Government integrity programs, which seem to have a pretty good record of being able to actually show dollar invested ends up resulting in \$8 to \$10 of savings?

Mr. DODARO. Yes, there needs to be more invested—probably in program integrity efforts, but the agencies really need to do a better job identifying the root causes of the problem. I do not think they have really done that much yet. I have asked for additional resources for GAO to help in identifying those things as well. But

there needs to be more analysis of what is actually causing the problems. There are some disputes associated with it.

But the other point I did not make in my opening comments—I will take this opportunity—is that these huge figures that I have quoted, over \$1 trillion, these estimates are not yet complete. There are no estimates for the managed care portion of Medicaid or the Temporary Assistance for Needy Families program. Other estimates are not complete or reliable. So this gives you an order of magnitude, but I think the problem is even bigger.

Senator WARNER. Well, I am going to vote at some point and get back for a second round. Thank you, Mr. Chairman.

Senator GRASSLEY. Mr. Chairman, could I have just one minute out of order?

Senator JOHNSON [presiding]. Absolutely.

Senator GRASSLEY. Because I want to compliment this agency for something dealing with the report that they are giving to us on financial management at the Department of Defense. So we passed a law, let us say, 6 or 7 years ago that the Defense Department services are supposed to be auditable by 2017. So then they start with the Marine Corps audit because it is the smallest, and there are all sorts of shenanigans going on over a period of 2 or 3 years to make sure that they are certified to be auditable. Well, it was—I do not know what adjective to use. It was just a fraud. And I asked this agency to look into it, and because of their hard work, they made the Defense Department withdraw the Marine Corps audit until it gets right so it can be audited. So I want to thank you for your work of exposing that fraud in the Defense Department.

Senator JOHNSON. Well, Senator Grassley, I certainly share your commendation of the GAO for doing that, but we have to commend you as well. I have to commend. You are the one that was a bulldog on that, so—

Senator GRASSLEY. Well, I gave a speech on it a year ago, but nobody reads your speeches.

Senator JOHNSON. It did always amaze me that, you know, rather than just do the audit, they, you know, went through the process of preparing for the audit. And I would say, you know, just cut to the chase and get right to the audit.

Mr. Dodaro, thanks for coming here today. I want to go to the exhibit that is actually the balance sheet, and I want to get to the sustainability measures. Let us first start out, though, because in your testimony you talked about how Treasury cannot eliminate transactions, how they are not very good at compiling.

A question I have asked of Government witnesses now eight times—this will be the ninth—has to do with the Social Security Trust Fund, which I have not looked at the most recent figure, but back the last time I asked, the trust fund had about \$2.7, \$2.8 trillion of U.S. Government bonds. So that is an asset to the trust fund. What is a U.S. Government bond to the Treasury?

Mr. DODARO. Pardon me?

Senator JOHNSON. What is the U.S. Government bond to the Treasury? It is a liability, correct?

Mr. DODARO. Right, right.



Senator JOHNSON. So if we consolidate the books of the Federal Government, you have got a \$2.7, \$2.8 trillion asset in the trust fund, you have got a \$2.8 trillion liability in the Treasury. What does that net out to?

Mr. DODARO. Zero.

Senator JOHNSON. Zero. So the trust fund to the Federal Government has no financial value. Is that a correct statement?

Mr. DODARO. The only thing—

Senator JOHNSON. Your microphone.

Mr. DODARO. I am sorry. The only thing that gets reported on the financial statements is the debt held by the public because the trust fund is an intragovernmental transaction.

Senator JOHNSON. But, again, if the Government is relying on the trust fund to fund the Social Security benefits, it is going to have to borrow that money again.

Mr. Dodaro. Yes.

Senator JOHNSON. The transaction financially nets to zero. So my question is: On the sustainability measures, exactly what is this—is this an unfunded liability? What is the calculation here? Is this coming right out of the Trustees' reports?

Mr. DODARO. It is usually in some of the Trustee reports, but also alternative assumptions, particularly for Medicare, for example, because even the Trustees do not believe that all the cost containment efforts under Medicare are going to hold over a period of time. So there is a difference of about \$8.9 trillion between the baseline estimates and the alternative estimates for Medicare.

But basically it is a projection of net present value of expected revenues and expenditures for the Federal Government, non-interest expenditures over the period of time, to show what the gap would be. And the gap is huge.

Senator JOHNSON. Right. So, basically, what you have got in Social Security, somewhere around \$13 trillion net present value, unfunded liability, and in Medicare you have got about \$28 trillion. Correct?

Mr. DODARO. Right. That is correct.

Senator JOHNSON. Do we by any chance have my one-page income statement on the screen? This is something that—and, actually, Senator Warner was a cosponsor, asking CBO to come up with kind of a one-page income statement describing the 30-year deficit. One of my problems when I came here as a business guy, you know, these unfunded liabilities, the public does not really understand net present value, and it just was not particularly relevant. So, actually, in discussions with the White House, I decided to describe the problem or define it as a 30-year demographic bubble, you know, what is—and I asked colleagues, what is the deficit over the next 30 years?

# INCOME STATEMENT for the federal government: FY2016 to FY2045

Congressional Budget Office's alternative fiscal scenario  
(dollars in billions)

	OUTLAYS			REVENUE			DEFICIT		
		% GDP	% total		% GDP	% total		% GDP	% total
Social Security	\$65,284	5.9%	21.7%	\$51,187	4.7%	25.8%	(\$14,096)	1.3%	13.7%
Medicare	49,219	4.5%	16.3%	15,569	1.4%	7.9%	(33,650)	3.1%	32.6%
	114,503	10.4%	38.0%	66,757	6.1%	33.7%	(47,746)	4.3%	46.3%
Outlays:									
Defense	37,151	3.4%	12.3%						
Nondef discretionary	36,251	3.3%	12.0%						
Medicaid/Obamacare	29,708	2.7%	9.9%						
Mandatory: other	28,785	2.6%	9.6%						
Interest expense	54,982	5.0%	18.2%						
	186,876	17.0%	62.0%						
Revenue:									
Individual income tax				101,935	9.3%	51.4%			
Corporate tax				17,189	1.6%	8.7%			
Excise taxes				3,706	0.3%	1.9%			
Estate and gift tax				1,004	0.1%	0.5%			
Custom fees, duties				2,486	0.2%	1.3%			
Miscellaneous rev				5,179	0.5%	2.6%			
				131,510	12.0%	66.3%			
				198,286	18.1%	100.0%			
<b>Total rev, outlays, deficit:</b>	<b>301,379</b>	<b>27.4%</b>	<b>100.0%</b>				<b>(55,367)</b>	<b>5.0%</b>	<b>53.7%</b>
<b>30-yr GDP: 1,098,100</b>							<b>(103,113)</b>	<b>9.4%</b>	<b>100.0%</b>

Source: CBO, Long-Term Budget Outlook, June 2015

Well, CBO actually does calculate this in projections, but they do it as a percent of GDP, so we converted these to numbers. And here are the stark results in a one-page income statement over 30 years. You have got a deficit—in other words, we are going to pay out more benefits in Social Security than we take in the payroll tax, about \$14 trillion, which kind of relates to the \$13 trillion unfunded liability.

Mr. DODARO. Right.

Senator JOHNSON. In Medicare, it is about \$34 trillion. Okay? And then the remainder of that—by the way, the deficit over the next 30 years projected by CBO is \$103 trillion, about \$10 trillion the first decade, \$28 trillion the second, \$65 trillion the third. It is comprised of \$14 trillion in Social Security, \$34 trillion in Medicare, and the rest is interest on the debt.

Mr. DODARO. Right, right.

Senator JOHNSON. And, again, that is what we are trying to show here with the balance sheet, and these numbers are just incomprehensible.

Mr. DODARO. Right.

Senator JOHNSON. So how do we convey in a more understandable way what you testified to, that this is completely unsustainable?

Mr. DODARO. Right. We have a graph in our testimony statement.

Mr. KING. Page 31.

Mr. DODARO. Page 31, Senator, I believe illustrates the problem. Thank you, Senator King. Right on time. These are our simulations of the long-term Federal Government's fiscal path. This shows under the baseline simulations that are under current law. This also has two important benchmarks: the historical average post-World War II of how much debt the government held as a percent of gross domestic product, 43 percent on average. Right now we are at 74 percent. We are very heavily leveraged in debt.

Under current law—this shows us hitting the historic high, the highest in the United States Government's history of debt held by the public as a percent of gross domestic product was 1946, right after World War II. We are on track to hit that in the next 15 to 25 years.

The alternative number at the top here assumes that the cost controls for Medicare basically do not hold over that period of time and health care costs go higher.

So we believe this illustrates that debt will continue to rise—these projections go to 200, 300 percent, and even higher, of debt held by the public as a percent of gross domestic product. We are going to owe more than our entire economy is producing, and by definition, this is not sustainable.

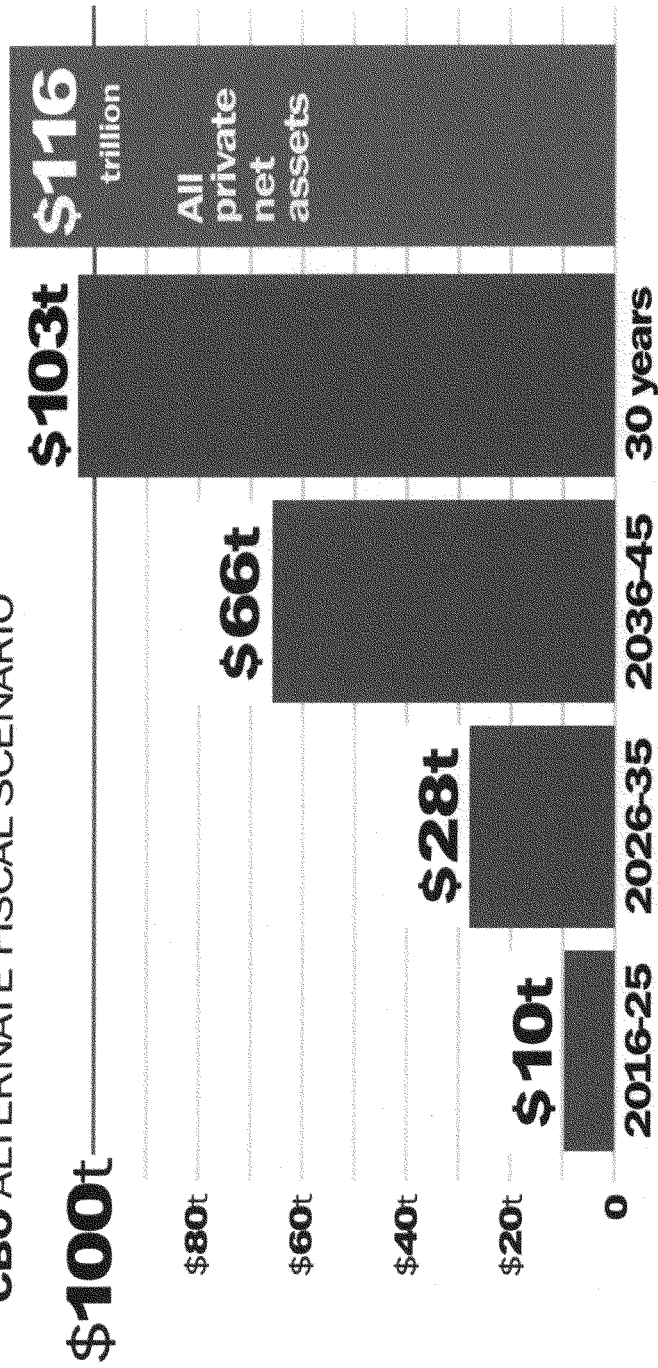
Senator JOHNSON. Right. Well, again, our total debt is about \$19 trillion. Tack on over the next 30 years \$103 trillion. I think that is the very definition of unsustainable.

Mr. DODARO. My basic point, Senator, is that you show it this way, you show it OMB's way in the financial report, you show it our way, you show it CBO's way, it all shows the same. It is unsustainable, and it needs to be addressed.

Senator JOHNSON. As I am turning it over to Senator Kaine, let us just put the 30-year deficit chart up there, which is a little more graphic. By decade, I think it is \$103 trillion, talking probably net asset base of America by comparison, I think it says 116. I do not have my contact in.

# 30-YEAR PROJECTED DEFICITS

## CBO ALTERNATE FISCAL SCENARIO



Congressional Budget Office, Office of Management and Budget, Federal Reserve

Senator Kaine.

Senator Kaine. Thank you, Mr. Chair, and thank you, Mr. Dodaro. We are really pleased to have you here. It is funny that Senator King pointed you to page 31, because I want to ask you about page 30 of your testimony in the same area, the same topic, really, long-term fiscal challenges, this pretty blunt quote: "Over the long term, at the Federal level, the imbalance between spending and revenue that is built into current law and policy is projected to lead to continued growth of debt held by the public as a share of GDP. This situation—in which debt grows faster than GDP—means the current Federal fiscal path is unsustainable."

I am interested in kind of getting your opinion on this issue, because it has puzzled me coming here, having been a mayor and a Governor, that we had debt policies in the city of Richmond and in the Commonwealth of Virginia. The number was not the issue. So I know trillion sounds like, oh, we cannot have a debt of a trillion. We never worried about the number, just the total amount of debt. What we worried about was two ratios, and the ratios were: debt to State GDP; and then also a very important one, which is interest payment as a percentage of the annual State budget. Those were the two ratios. And in both the city and the State, we managed to those ratios, and that is how, when we went up New York and talked to the bonding agencies, how are you doing with respect to your basic management. So they did not worry about the raw number. They worried about the ratio.

I have been interested, being on the Committee here, that we do not have an agreed-upon ratio. Obviously, if you have a ratio, there is plenty of grounds for difference of opinion about how to get there. So do you get there for more revenue. Do you get there through expense cutting? So there is plenty of play for policy differences, but we had a bipartisan consensus in both bodies about what the two ratios would be that we would manage to, and then over time we managed to that.

We had a hearing about a year ago in this Committee that was called "America's Dangerous Debt," and I asked each of the three witnesses, "What level of debt is dangerous?" And none of them would give me an opinion. They all just assumed we have dangerous debt, but they would not give an opinion. And I said, "Well, gosh, maybe no wonder that, you know, Congress does not have an agreed-upon policy about ratios we will manage to if the experts that appear before us will not even give us an opinion."

Now, you in this paragraph talk about debt to GDP average post-World War II, 46 percent. Of course, much of the post-World War II average was before Medicaid and Medicare, the programs of the 1960s that we have supported over the years.

Mr. DODARO. That is correct.

Senator Kaine. And yet, nevertheless, the historic average can be really important. I would be kind of curious as to what would be the historic average post the adoption of Medicaid and Medicare. That might be more relevant. But we can get into that in a minute.

Do you think it would be a good idea for Congress to have a debt management policy that would be focused on equivalent ratios, debt to GDP, and the percentage of income in a given year that we are putting to debt service.

I always look at the debt service payment as, you know, we are paying this sort of for decisions in the past, and it is taking away from what we can do in the future. Now, that was definitely the case in the city and State where you only used debt for capital expenditures. We did not use debt for operations. So some of debt payments is for current operations, but when you pull debt service payment out, it is restricting what you can do currently, and I still kind of look at it that way.

Would there be a way, you know, from an economist's standpoint or an accountant's standpoint, to come up with ratios that would be meaningful in a budget like—a Federal budget that has a printing press, that has monetary policy? Or is that a concept that, frankly, is more meaningful for a State government and not so meaningful for a national budget?

Mr. DODARO. No, I think it makes a lot of sense for the Federal budget, and I would encourage Congress to do this. You know, the debt management issues at the Federal level have never really been modernized at all. Prior to 1917—and I was not in my job then. [Laughter.]

Senator KAINE. It sometimes feels like it.

Mr. DODARO. Yes, right. But Congress approved every debt issuance, but in 1917, World War I came, and then it became impractical. So the government moved to the current approach of setting a debt limit, but that is way too late. It is after the spending decision has already been made.

Senator KAINE. Yeah, and the debt limit, again, is a raw number, and no smart fiscal manager uses a raw number as a check.

Mr. DODARO. Right, right.

Senator KAINE. You use a ratio as a check.

Mr. DODARO. Right, you use the ratios. I think it would have to be a policy decision on the ratios. I think you would have to allow for exigent circumstances.

Senator KAINE. Right, time of war.

Mr. DODARO. Time of war, economic downturns, whatever you want to put in there. But you would have something to manage to. Right now there are not ratios to manage to from the debt standpoint. We manage on how much spending that we want to have on an annual basis, but that really does not deal with the long-term circumstances.

These numbers we have been showing, by the way, do not include any potential expenditures for disasters, for economic downturns, for any other emergencies that may come up. And so I think it makes eminent sense, and we have looked at some other countries. I think Sweden and some of the other countries do set limits. They do set debt-to-GDP ratios that they manage to as a country. So it makes sense on a national level.

What we have now does not make sense, so we need to do something different. I think that offers a good alternative.

Senator KAINE. Well, that is good encouragement. Thank you. And I will return it to you, Mr. Chair.

Chairman ENZI [presiding]. Thank you. And I think Israel probably has that formula, too. I think they have shared that with us.

Senator Ayotte.

Senator AYOTTE. Thank you, Chairman.

I want to thank you, Mr. Dodaro, for all your important work, and I wanted to ask about the improper payment issue because, as I look at your report, you say in the report on page 20, "In fiscal year 2015, agencies reported improper payment estimates totaling \$136.7 billion," and I believe in your testimony you highlighted it could be as much as \$1 trillion as we look at improper payments. Is that true?

Mr. DODARO. It is over \$1 trillion that has been reported since 2003.

Senator AYOTTE. Oh, since—okay.

Mr. DODARO. That is the cumulative amount. The 136, is the latest annual reported amount.

Senator AYOTTE. Okay. I am glad you clarified that. But I think one of the biggest things we could be concerned about—I mean, obviously, that is a huge amount of money, \$136 billion. Do you know what we could do for that in terms of the defense and the military? We are actually giving pink slips to our members in our army right now, the threats we are—whatever your issue is in this Congress, it seems to me this should be something we would focus on, whatever you think Federal spending should be, and obviously dealing with our debt.

So I wanted to ask you, you said in the report on page 20 that essentially this has been a "significant increase" in 2015 of improper payments, over \$12 billion, mainly due to an increased error rate in Medicaid—from the prior year's revised estimates.

So if you could tell me what you think is the source of that driver in the increased error rate in Medicaid, but also, I was very interested on the same page you said that 76 percent of our improper payments are made up from improper payments for Medicare, Medicaid, and the Earned Income Tax Credit. So what do you think is driving the increase in Medicaid, number one? Is it the Affordable Care Act and also the fact that there has been all kinds of issues in terms of people's income verification and the inability to determine in some ways, you know, who is eligible and who is not and clearly communicate that with taxpayers? That is certainly an issue I have addressed in other committees.

And then also, as I look at Medicare, Medicaid, and the Earned Income Tax Credit, what should we be doing? This is a huge, huge amount of money. If we just focused on this issue, we could save billions of taxpayer dollars.

Mr. DODARO. Yes, first on Medicaid, what is primarily driving it is the amount of changes that have been made in the programs, and the States do not have the systems yet put in place to verify eligibility and to include changes. Some people move from the exchanges to the Medicaid program and back, and so that is a big problem.

But I would also point out on Medicaid, this improper payment rate does not even measure the managed care portion of Medicaid in the States. We have encouraged and CMS is going to now audit. The only thing they look at now is whether the State is paying the Medicaid managed care provider properly, not whether the provider is actually making payments that are consistent with the rules and techniques.



We have also been trying for a decade to get CMS and they finally have agreed—to take the Social Security numbers off Medicare cards. This prevents identity theft and easy identification.

Senator AYOTTE. Right.

Mr. DODARO. Congress fortunately passed a law, gave CMS funding, but it may take them, according to their estimates, 2 or 3 years to have that happen. They are also not analyzing post-payment claims where they go in afterwards and identify problems and patterns and share that among the contractors, embedding it to try to prevent improper payments from occurring in the first place.

Also, they are allowing providers to enroll but not always determining whether they are legitimate providers by using all potential methods to do that.

Senator AYOTTE. Yeah, they are not using even all the publicly available data, are they?

Mr. DODARO. That is correct. For example, physicians who might have had license censures in other States, they are not sharing that information properly.

So we have made lots of recommendations on how this can be improved. The programs that you mentioned there, particularly the health care ones, are the fastest growing Federal programs. Unless we get on top of this, in my opinion, this problem could potentially get worse before it gets better.

Senator AYOTTE. And it is huge right now. It is unbelievable. The other issue is that the right hand often is not talking to the left in terms of our ability to share information for eligibility across programs within our own Government. Isn't that still lacking?

Mr. DODARO. Yes.

Senator AYOTTE. So, for example, I may be eligible for one Federal program, but not for the other, and we are not sharing that information.

Mr. DODARO. That is correct. And, in fact, we have asked for special legislative authority. There is what is called the "New Hire Database" that HHS maintains for child support enforcement, and they will not share that information with us, and they will not share it with other agencies as well. And that database includes some of the most recent wage information. So programs that are based on income eligibility could use that information.

Senator AYOTTE. So you need our legislative authority to do that? That is what you need?

Mr. DODARO. Yes. We believe we have it. The agency believes that—

Senator AYOTTE. But the agency does not believe you have it?

Mr. DODARO. Does not believe we have—

Senator AYOTTE. So we need to clarify that.

Mr. DODARO. Yes.

Senator AYOTTE. Okay. Thank you.

Mr. DODARO. Yes, that would be very helpful.

Senator AYOTTE. Thank you very much.

Chairman ENZI. Thank you. I am sorry that I missed part of this, but I will go back and gather information from that. I have been trying to get a capital budget since I got here, and we have come close a couple of times, but close does not do it in budgeting. The

Federal budget process, of course, treats the capital investments the same as any other kind of spending. I guess you could call it “cash accounting” for huge infrastructure. It creates a bias against capital spending since its full costs are recognized up front, but the benefits are over time. Therefore, some would like to see at least an element of capital budgeting injected into the budget process.

Unlike States and localities, the Federal Government owns only a small fraction of its capital investments, and these items are considered Federal capital. On the financial statement GAO reviewed, the Government reports owning property, plant, and equipment valued at \$894 billion. To have an effective capital budget, you need to know what you own, its condition, and its deferred maintenance needs. It appears from your audit, though, that we lack reliable information about what the Government owns and what condition it is in.

Isn't the unreliability of the Federal property inventory one of the reasons GAO did not deliver an unqualified audit opinion? Do you agree we need a reliable accounting of what we own and its condition so that we can have an effective capital budget for the Federal capital?

Mr. DODARO. Yes, definitely. It was one of the reasons that we were unable to give an opinion, largely as a result of the property, plant, and equipment, and inventories at the Defense Department.

The other thing I would point out, Mr. Chairman, is that since 2003 we have had Federal real property management as a high-risk area across the Federal Government. There is a lot of bad information that is not only in the Defense Department but in the civilian agencies about what we own, where it is, what condition it is in, and how it is being utilized. And so this remains a high-risk area across the Government, and it needs to be dealt with.

Chairman ENZI. Thank you. Among other material weaknesses with the financial statements, you cite concerns regarding the tax collection activities. I quoted earlier, and I will quote again, “Due to the financial system limitations as well as errors in taxpayer accounts, the Federal Government’s records did not always reflect the correct amount of taxes owed by the public to the Federal Government. Such errors may cause undue burden and frustration to taxpayers who either have already paid taxes owed or who significantly owe lower amounts.”

Can you talk a little bit about the extent of this problem, how the taxpayers’ accounts are impacted, how the situations are resolved? Does the IRS have a process when it attempts to identify and correct the errors on its own?

Mr. DODARO. Basically, they have a process to make assessments. They do not have a subsidiary ledger for every taxpayer with exactly what they owe, and that is part of the problem. So in order to come up with this, they have to do statistical samples. But, basically, if there is an error in a taxpayer account, the burden is on the taxpayer to deal with the IRS to resolve the issue.

IRS had to make, in order to get a reliable number, about \$9 billion in adjustments to their receivables number. They need to have better systems in place, and we have encouraged them and recommended that over the years. But for right now, they do not have at the ready accurate information on individual taxpayers to the

point that you really need to in order to efficiently and effectively manage the system, and it puts an undue burden on the citizens.

Chairman ENZI. I think in this electronic age that that is something that could be taken care of. Are they on any kind of a track to do that?

Mr. DODARO. They have system plans to do it, but their track record has been a little spotty over the years on whether they can actually bring those changes to fruition. But we continue to monitor that. I would be happy to provide some additional information on that for the record.

**Additional Information for the Record Requested at the April 6<sup>th</sup> Hearing**Insert for Transcript – pg. 39

The Internal Revenue Service's (IRS's) balance for federal taxes receivable,<sup>1</sup> which comprised over 80 percent of total assets reported on IRS's fiscal year 2015 balance sheet, was not produced from its general ledger through the summation of taxpayer account transaction data,<sup>2</sup> but rather was the product of a compensating, labor-intensive, and manual estimation process.<sup>3</sup> This process is necessary because limitations in IRS's financial systems and errors in taxpayer accounts render its systems unable to readily distinguish between taxes receivable, compliance assessments, and write-offs in order to properly classify these components for financial reporting purposes. Absent the use of this statistical estimation process, the various unpaid tax assessment balances produced by its subsidiary ledger may have been materially inaccurate, and IRS had no other means of evaluating the accuracy of these balances. However, since IRS derives the taxes receivable balance reported on its balance sheet and the balances of compliance assessments and write-offs reported in its required supplementary information (RSI) from the results of this estimation process rather than from the general and subsidiary ledgers, it cannot trace these amounts through its general ledger system, and back to underlying transaction-level taxpayer source documents. Such traceability is necessary to enable IRS to ensure that recorded transactions are complete, accurate, and supported by underlying records.

In response to our recommendations from prior audits, IRS has taken actions over the years to improve its management and reporting of unpaid tax assessments. Among these actions, IRS documented its plans for addressing its system limitations in its Federal Financial Management Improvement Act remediation plan and a long-term action plan that it formalized in 2015. Both plans discuss the phased-in implementation of its Customer Account Data Engine 2 (CADE 2) as a key component to resolving the material weakness over unpaid tax assessments.<sup>4</sup> IRS expects the enhancements from the second phase to allow its financial systems to record and produce more accurate information for financial reporting purposes. However, according to IRS's most recent Information Technology Investment Report,<sup>5</sup> it doesn't expect to complete the second phase until 2020.

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<sup>1</sup>IRS reports federal taxes receivable on its balance sheet, net of an allowance for uncollectible taxes receivable.

<sup>2</sup>For financial reporting, in order to reflect its compensating statistical estimate for its gross taxes receivable amount, IRS records an adjusting journal entry to correct the gross taxes receivable amount produced by its systems, and then reduces the adjusted gross taxes receivable amount by an allowance for uncollectible taxes receivable to report the amount of net taxes receivable on its balance sheet.

<sup>3</sup>This compensating process involves IRS testing statistical samples of data extracted from its master files and extrapolating the results to estimate the year-end balances to be reported as (1) taxes receivable in its financial statements and the RSI and (2) compliance assessments and write-offs in the RSI.

<sup>4</sup>IRS expects CADE 2 to deliver its functionality incrementally through the completion of two transition states and a target (final) state. CADE 2 is a program created for processing individual taxpayer accounts that is intended to replace IRS's current outdated program – the Individual Master File. IRS's master files contain detailed records of taxpayer accounts. IRS has one master file for individuals, and another one for businesses.

<sup>5</sup>IRS is required to submit a quarterly report to the Committees on Appropriations of the House of Representatives and the Senate, and the Comptroller General of the United States detailing the cost and schedule performance for its major information technology investments including CADE 2. See the Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division E, Title I (Dec. 18, 2015). The most recent report IRS submitted is for the quarter ended December 31, 2015.

Furthermore, even when fully implemented, CADE 2 will not completely resolve the deficiencies related to IRS's reporting of unpaid tax assessments because CADE2 is designed only to replace the master file that retains individual taxpayer data, and not the business taxpayer master file. Resolving these deficiencies requires IRS to address issues in both master files.<sup>6</sup> Therefore, it is unclear when IRS will fully correct the issues that cause significant inaccuracies in the unpaid tax assessments information maintained in its accounting systems. We continue to monitor IRS's progress through the work of various GAO mission teams, including the Information Technology team, which follows- up with IRS on a quarterly basis and the Financial Management and Assurance team's annual audit of IRS's financial statements.

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<sup>6</sup>While IRS's long term action plan discusses actions to improve reporting on business taxpayer accounts that are not within the scope of CADE 2, it is unclear when IRS would complete such actions because IRS did not include milestones or target completion dates for most of these actions, but rather indicated that completion is based on IRS's priorities and available funding.

Chairman ENZI. The financial statements you audited contain data concerning the Government's long-term fiscal sustainability. I suspect that Senator Johnson asked some questions about that and had a few slides. He is really concentrated on the long term. Your reports show that the Federal Government under current law is in a \$41.5 trillion hole over the next 75 years with regard to Social Security and Medicare, with two-thirds of that total relating to Medicare. That \$41.5 trillion is the present value of the future expenditures in excess of future revenue dedicated to these programs. But according to the GAO audit report, the \$41.5 trillion may understate the crisis because it is based on uncertain reductions in future Medicare cost growth.

Do the financial statements give an indication how much deeper the Government would be in the hole with respect to Medicare if the anticipated reductions in cost growth assumed under current law are not achieved? Is there any speculation on that? What does your report tell us about—

Mr. DODARO. Yes, there is disclosure in the financial report about an alternative projection that shows, if those Medicare costs are not contained over time, what the additional costs would be. It is \$8.9 trillion. That is on top of the \$27 trillion that is already included in the baseline estimate. So it is significant.

Chairman ENZI. Yes. It is much easier to talk about trillions than it is billions. They do not sound like nearly as much. I have been trying to get people to relate to a trillion being a thousand billion. It sounds like more.

Mr. DODARO. Right.

Chairman ENZI. Thank you.

Senator King is back. Senator King.

Senator KING. Yes, thank you, Mr. Chairman.

One of the issues you note in the report is the cost of the debt limit process or non-process around here. You estimated it cost between, I think, \$38 and \$70 billion.

One of the alternatives to the process that we have now, it seems to me, is some variation of what is called the "Gephardt rule," which used to be the case in the House where, if Members of Congress vote for a tax cut or an expenditure that has an effect on the debt, the debt limit is automatically extended in order to cover that change, because the process we have now allows us to have it both ways. We can vote for the expenditure, vote for the tax cut, and get all that political credit, and then vote against the debt limit and call ourselves conservative.

Thoughts on improving the debt limit process?

Mr. DODARO. Yes. One of the issues Senator Kaine discussed that I would mention about managing the debt would be to set some potential ratios on debt held by the public as a percent of gross domestic product as a target that you work against. So you can improve the current process, and we have some ways to do that. You can link it to the budget resolution process so at the time spending and revenue decisions are made by the Congress, there is a recognition that there is a gap and there is going to have to be money borrowed, just the way you would in your household budgets.

You could allow the executive branch to borrow the money necessary and submit a resolution; the Congress would have to disapprove the borrowing.

You could allow the administration to borrow whatever is needed in order to effectuate decisions that the Congress has made.

But you could also, in terms of managing the cost of borrowing for the Federal Government, set some limits on debt as a percent of gross domestic product as a target to work against.

Senator KING. Or debts in the States. In our State, the number we looked at was debt service as a percent of the budget or debt service as a percent of GDP.

Mr. DODARO. Right. You could do that. Senator Kaine mentioned that, too. So there are a couple measures that could be used. Other countries use those measures.

Senator KING. Well, in terms of your auditing and trying to make sense of the Federal budget, one of the things that strikes a person who is sort of new to this process is that there is no capital budget. There is no distinction between paying a park ranger and buying a building or a 40-year submarine. It seems to me that that would be a reform that would clarify the accounting, because we are paying for capital assets the same way we pay for current operations, and it obscures the true picture of where we are.

Some part of this debt is justified as long-term capital investments. The part that is not justified is the debt that we are taking on in order to pay operating expenses. Your thoughts on that?

Mr. DODARO. I think there are definite advantages to the unified budget approach that we have in place, and so I would want us to maintain that because it gives a total picture on the debt ceiling.

Senator KING. Right.

Mr. DODARO. But within that—and we have done some analysis of alternatives—there could be an investment component. Now, that could include not only capital assets, but the Federal Government also makes a lot of investments in both human resources and in other areas where there are economic benefits as opposed to initial outlays to provide services to people. So you could construct within a unified Federal budget an investment component that would allow for more discrete decisionmaking about the types of spending that the Federal Government is going to have and what the expected outcome would be and what could be done in order to better manage this.

For example, we have made recommendations that I will provide for the record here on how the Federal Buildings fund could be used better in order to effectuate these types of decisions.

Senator KING. Let me interrupt because I am limited on time. Your chart on page 31 that shows the projected debt limit, the heading is “Debt Held by the Public.” That does not include the Social Security Trust Fund obligation back to the Federal Government. Is that correct?

Mr. DODARO. Well, it shows the cash flows for revenues going back and forth. So, the mechanics of it is that the Treasury securities held by the Trust Fund would have to be redeemed, as they have been since 2010 on Social Security, because the outflows are more than the payroll taxes coming in. So it would assume—it would account for—

Senator KING. That assumes the payment of those debts.

Mr. DODARO. Yes. Plus it assumes continued payments.

Senator KING. Do you know what GDP growth assumptions are in this?

Mr. DODARO. I think it is roughly 2 to 3 percent.

Senator KING. Okay.

Mr. DODARO. But I will provide the details for the record.

Senator KING. But I would also point out that there is another deficit that is not shown on this chart, which is the infrastructure deficit. As a Governor, I used to go and talk to the rating agencies about trying to get a lower interest rate, and one of the analysts made the point to me that if you are not fixing your infrastructure, that is a form of debt just as if it is debt on the books. And if we are not maintaining our infrastructure and focusing strictly on these numbers, we are missing an even larger number that is part of our overall debt burden.

Mr. DODARO. Yes, that is exactly right, because you are going to have to fix it at some point, anyway.

Also, what is not in here is planning for natural disasters, and economic downturns. But in relation to transportation, we have had financing the Nation's transportation infrastructure on our high-risk list for many years now because we do not have a means of doing it. It could be a component of this investment approach that you could have within the budget.

Senator KING. Mr. Chairman, I am over my time, but one, I think this could be a 10-second answer. How much Federal revenue is not collected each year under the tax system?

Mr. DODARO. The latest estimate from IRS—annual figure based on a 2006 analysis is a \$385 billion net tax gap between taxes owed and taxes collected. We have about an 83-percent voluntary compliance rate right now in our country.

Senator KING. But I would point out, of the \$385 billion, it is very close to the total of our current deficit. If we just collected the taxes owed, we would almost eliminate the current deficit.

Mr. DODARO. Well, yes. I mentioned we also have \$136 billion in improper payments made last year as well, payments that should not have been made or that were made in the wrong amount. So, it is not going to solve our problems, but it would make it a lot easier if we only paid the correct amount and we collected everything that we were supposed to.

Senator KING. Thank you.

Thank you, Mr. Chairman.

Chairman ENZI. Senator Perdue has returned, so he will be next, and then Senator Warner and then Senator Johnson.

Senator PERDUE. Well, thank you, Mr. Chairman. I am not an accountant, but I will agree with you that this is an exciting meeting. I did serve on several audit committees of large public corporations, so I know how important it is when you are making business decisions to have accurate information, and I applaud you, Mr. Dodaro, for what you are doing. I think this is so critical to us as we start looking at the process and try to get a long-term strategy to bring this debt more under control.

I agree with Senator Warner and Senator King. We have had these conversations before, and this is not a partisan issue. That



is the encouraging thing about it. This is not about how you spend money or how you cut expenses or whatever. This is about getting an accurate reading of what we are doing.

And so my observation—and I have got a couple of questions I would love to get your thoughts on, because it is going to be an ongoing dialogue here. This is not something we are going to have a hearing on and then forget about it, because I am absolutely committed, as is the Chairman and other people, you can see that you have got people who have been sitting here for 2 hours or over an hour and a half now trying to move this thing forward.

But since the Government Management Reform Act of—it was 22 years ago, and 20 years ago the first publication of the consolidated financial statement, we are sitting here today—and this is not a critique on you. It is the systems. You mentioned DOD. We still do not have an accurate balance sheet that would stand up to audit.

Mr. DODARO. Right.

Senator PERDUE. I find that remarkable. And our goal should be to solve that as soon as possible, and I am going to have a question, then I want to come back. But I just look at redundant agencies, improper payments, and taxes not paid. You know, my math is that is \$500, \$600 billion. You add this up, pretty soon you are talking about serious money. Well, I do not know why we do not shut the trains down going to the Capitol. I do not know why we do not just shut everything else and focus on—this is not about cutting Social Security or doing anything else. This is just prudent, responsible stewardship of taxpayer money. This is not a small thing. And I know you know that. You are preacher for that. I am just voicing one person's—and I think I speak for a few other members here—support to try to help you get there.

I am worried about accrual accounting versus cash accounting, and therein lies another disparity of almost \$100 billion of difference between the GAO estimate of an annual deficit and other estimates of the annual deficit. There is no capital budget. I think Senator King talked about that, and I agree 100 percent with Senator King that if you do not maintain—it is like deferred maintenance. If you do not spend that money on maintenance every year or on infrastructure, that is a future unfunded liability, is the way I look at it. And so we do not talk about that as well, but that is the second step.

DOD, right now DOD is somewhere around \$600 billion. People say, well, that is just too large to audit. Well, Wal-Mart is not much smaller than that. As a matter of fact, it is pretty close to being about the same size. Imagine if Mike Duke or any of the other leaders down there came to the SEC or the IRS and said, "Boys, I am sorry. We are just too big to be audited. We will defer next year." I do not think that would work very well. And so I am over this "too large to be audited" thing, and so it is time we get a real accounting of that. Long-term debt, it is just unsustainable. It is the reason we are starting this process.

So the question I have is: What do we have to do to help you break through the impediments to get a consolidated balance sheet that can stand up to audit?

Mr. DODARO. Well, I think there are two other things. You mentioned DOD, but there are three main impediments to us giving an

opinion on the consolidated financial statement of the U.S. government.

Senator PERDUE. But it is much bigger than DOD, though.

Mr. DODARO. Pardon me?

Senator PERDUE. It is much bigger than DOD. I mean, they are one of the largest culprits, but there are other large agencies as well.

Mr. DODARO. Well, actually, that is the bright spot in this picture. When we first started in 1996, that was the first year that all 24 major departments and agencies had to prepare statements and have an audit. So we went 200 years of our history without an audit. Even though the Federal Government used to not give the State and local governments money unless they had an audit, but that is a different story.

Right now, this past year, 21 of the 24 CFO Act departments and agencies have been able to get a clean opinion.

Senator PERDUE. You said that, yes.

Mr. DODARO. The two, aside from DOD, that did not get a clean opinion, HUD and Agriculture, have had clean opinions in the past. So they have had some recent problems. The Department of Homeland Security was an outlier for years, but for now, the last 3 years, they have had an unqualified opinion. So, really, when you look at the major departments and agencies, DOD is the one, is the only one.

Senator PERDUE. That is encouraging.

Mr. DODARO. But they hold about 30 percent of all the Government's assets and about 15 percent of its net costs.

The other problems are at the Treasury Department working with the agencies where there are hundreds of billions of dollars of activity among the Federal agencies that cannot properly be eliminated. Right now, because of that, there is a very polite line in the statement that says unmatched disbursements and transactions. Basically, it is a plug figure for things that they cannot account for properly to make the statements balance. But it is not accurate, and so that is a big problem. And there are still problems in compiling the information from the audited financial statements of the agencies with Treasury's process. So DOD really is the main obstacle along with these other processes.

Now, Treasury has a good plan——

Senator PERDUE. Sorry, I am out of time.

Mr. DODARO. Yes, go ahead.

Senator PERDUE. But I want to ask you, I understand there is a problem. My question is: What can we do to break through the impediment to get a balance sheet that will stand up to audit?

Mr. DODARO. Yes, I think you have to help us hold DOD accountable for making progress.

Senator PERDUE. They are working on it right now.

Mr. DODARO. They are working on it, but they are not really fixing the underlying problems. They have a good plan for the first time. You know, right now, the last year, in 2015, the only audits they had of Army, Navy, and the Air Force were 1 year's budget activities, and they were not able to pass the test of an audit on 1-year budget activity at the Department. The financial require-

ments are for a multi-year budget audit. They have not even started on a balance sheet or net cost statement as well.

The auditors this year made over 900 specific findings and recommendations for things that need to be fixed. That is on top of everything GAO and the IGs have said. They have to fix the underlying problems. They do not have necessarily all the talent that they need and experienced people. Congress could help there. They need to be held accountable for their system investments. They continue to make system investments that do not produce better systems. But they are not fixing the internal control problems. They cannot reconcile their balance between what they say they have and what Treasury says that they have. They are not estimating environmental liabilities properly, and they have a huge potential exposure there in addition to the Energy Department.

So there are fundamental problems. They have anti-deficiency violations. They have had about \$1 billion of anti-deficiency violations, where they were spending money that they should not have been spending in those areas. So this should be of concern to every member of Congress. We could use your support in helping them get the resources and the incentives necessary to make the necessary changes.

Senator PERDUE. Well, thank you, and I look forward to working with you on this.

Thanks, Mr. Chairman.

Chairman ENZI. Senator Warner.

Senator WARNER. Thank you, Mr. Chairman. I just want to follow up on, I think, a very good line of questions Senator Perdue made. The DATA Act that we passed is not going to solve the whole problem, but if you do not even have common definitions, the ability to come in and do an audit is basically moot. So, you know, the DATA Act was as bipartisan as you can get. If we strangle off the \$50 million of implementation money, we are not going to make sure that this gets done.

Now, we can argue, you know, should you be able to do it within the existing budget lines, but, you know, \$50 million compared to what we spend normally to actually get a common set of definitions and some more financial transparency, you shine a little sunlight on this with a common defined definitions, and I think you are going to have a lot more pressure.

So I would urge anybody who wants to join on the letter I am sending to all the 37 agencies to say get your plans, make this a high priority. GAO has been great at being the watchdog on this, but we are going to miss an opportunity here. And as the Comptroller General has said, this is not going to be fully implemented under this administration. Let us make sure that it actually continues to be a priority. And I really appreciate, Gene, again, your work in helping us at least get through the definitions and some more transparency. Two hundred and twenty different financial systems just in DOD, that is crazy.

I think we have got a lot of common agreement here. I think we have almost all said capital budgets—Senator Kaine has mentioned it. I support it. Former Governors, we ought to see what we can do there. I would argue that—and I know Senator Johnson has talked about this in even a broader scope than I have at times. You

know, we can debate about what was the causation of the deficit on an annual basis. It is coming down a little bit. But I think the problem is, although it is about to ramp right back up, we should at least acknowledge that the total aggregate debt both parties have got their hands on. And whether we call it at \$18 trillion or \$19 trillion at this point, you know, this is totally being masked in terms of its effect on our economy and the Federal Government operations because of unprecedented low interest rates. The factoid of a 1-point increase in interest, \$120 billion, yeah, that is a linear equation. It is actually a little bit on the low side because the debt rolls over. That is a safe estimate from even an accountant's standpoint. And that, you know, spends us a ton of dough, and we really need to look at that and, you know, remind ourselves that, as we all applauded ourselves getting out of town at the end of the year, to Senator King's comments about not paying for expenditures we put into law, many of them good provisions, \$600 billion of permanent tax cuts totally unpaid for wiped out most of the benefits we got from sequestration.

I would love to get some specific examples. We all know around improper payments and failure to share information between particularly in the health and welfare side. Give us guidance on how we can—Senator Ayotte was talking about this—what legislative items we need to do. I know there are HIPAA issues and other privacy concerns. But I really hope you give us some at least low-hanging fruit about sharing that information, not just with you but also that we ought to have access to.

My question is, you know, one of the areas of domain that I think is going to get exponentially worse is cyber. And, you know, I have got a lot of Federal employees, but the amount of angst and anguish still around the OPM data breach is just enormous. And I would like you, Mr. Dodaro, to comment a little bit. You know, GAO pointed out this around information security back in February 1997 before cyber became a big issue. You know, I would argue a lot of this is because we have got legacy IT systems that we never replace, that we simply patch one time after another, making more vulnerability.

I would also commend everybody's review, there is a group that has been stood up called "18F," kind of a SWAT team of folks that came from the Valley that are looking about how you do acquisition and development of IT systems the way the private sector does, particularly, you know, if you think about the large enterprises—Senator Perdue mentioned Wal-Mart. You know, Wal-Mart has got as complex of IT systems and purchasing as any entity in the Federal Government. They do not have—they have got some of the same vulnerabilities, but they can renew their systems in ways that the Government cannot, and we ought to look at that.

Can you speak for a moment about—my understanding is that when you go in and look at information security, you do manual audits. You have got kind of qualitative questionnaires. You kind of do one-off items. What can we do to help give you more tools around the whole information security, cybersecurity area?

Mr. DODARO. Well, in the last year, Congress passed about four different bills on cybersecurity. Here is the fundamental problem, though. As you pointed out, we raised this as a government-wide

issue. It is the first time we ever said anything across the entire Federal Government is high risk and we did it in 1997. We worked with the Congress to pass the Federal Information Security Management Act, and recent changes were just made to that act. But Congress has to hold the agencies accountable. They do not have in place agency-wide information systems that provide the proper amount of security, risk assessments, how to mitigate risk, and how to provide awareness to their employees.

A lot of the risks are employees accidentally clicking on links that they should not that downloads malware, or they bite on phishing expeditions by hackers and give up information. The agencies do not have good risk mitigation approaches in all cases—or remediation plans for how they are going to fix the problems, contingency plans, and also deal with the legacy systems.

Some of these legacy systems are decades old, and we are producing a report right now. We are working on an audit where we are listing the longest, oldest systems in the Federal Government. It will be a great surprise to a lot of people in terms of how old these systems are. This was before security was brought in, built in up front into these systems. Agencies also need continuous diagnostic and monitoring efforts. DHS is giving them some additional tools and techniques. They need additional talent in the agencies. The personnel classification approaches for cybersecurity analysis is not contemporary and up to date in order to make it easy to hire some of these people, and they may need some additional authorities.

But it is a management problem. There are technical issues, but it is largely a management problem.

Senator WARNER. My time is up, but Chairman Johnson did a good job in terms of taking some ideas that we had from the intel community to give on the dot-gov regime DHS the same ability to enforce that NSA has on the dot-mil side. I mean, one of the remarkable things that came out after OPM was a lot of the Federal agencies had basically ignored any of the advice from DHS.

Mr. DODARO. Right, and we had suggested that that be clarified. And one point I might make, if I can, Mr. Chairman, on the issue about working on a bill on the national hire database to share information, we have been working with Senator Tester and Senator Sasse. So if anybody wants to work with them, we would appreciate it.

Chairman ENZI. Senator Johnson.

Senator JOHNSON. Thank you, Mr. Chairman.

You know, part of the problem is GAO does great work, issues all these reports. The Inspectors General do great work, issue all these reports. OPM had those studies on their information technology systems, how high risk they are, and they just ignored it. And that is part of the problem.

The solutions in terms of management, providing information, you know, instituting controls, like Senator Perdue was talking about, Wal-Mart has got to have an audit. They have financial systems that work. So these things are available. We are just not accessing them in the Federal Government. That is certainly what drives me nuts.

Something else that drives me nuts, every time I hear that Congress has the power of the purse, I want to talk to you a little bit about that, because that is one of the controls that we have given away.

Last year, 62.3 percent—no, 68.3 percent of the Federal Government expenditure was mandatory. It is not appropriated; it just is mandatory. So less than a third of the Federal budget is actually appropriated and under some level of control, but even then, we noticed when the Government shut down in October, did you ever do any study in terms of exactly how much the Federal Government actually shut down when we were supposedly shut down?

Mr. DODARO. Yes. Yes, we did.

Senator JOHNSON. So how much actually shut down?

Mr. DODARO. Well, a good bit of it, but it was not as big of an impact as I think people estimated it to be because some agencies were reinstated during the shutdown. There were some disruptions with grants and contracts and other things.

Senator JOHNSON. But, again, you have got more than two-thirds mandatory that got spent. The Department of Defense, because it is essential, that continues to go, the Department of Homeland Security. The agency spending tied to the mandatory, there have been decisions that say that is also spent. So, you know, I have always thrown out probably less than 10 percent of the Federal Government actually shut down. I know there were some wayside rests in Wyoming that they chained off. We shut down the World War II Memorial.

So the bottom line is we do not have that control anymore because we do not have the budget really on budget. We have so much off budget.

Wouldn't that be also one of those common-sense reforms in terms of management to put the Federal budget on budget so that everything has to be appropriated every year?

Mr. DODARO. I would certainly think that that would be a way to exercise better control. Offhand, I do not see any downside to doing that. I think it would impose greater discipline on some of these other programs, but I also think that the Congress should set some policies on how much borrowing collectively we should do as a Nation and then from there allocate the resources.

And I agree, even on Medicaid, for example, right now the CMS at HHS is approving waiver demonstrations to allow States to experiment. Almost a third of the spending now on Medicaid went around the Congress because of that. And these demonstrations were supposed to be budget neutral, but they were not when we looked at them.

So I think there is not adequate control by the Congress on a great deal of these activities.

Senator JOHNSON. Have we discussed multiple-year budgeting here? I know I was out for votes. I think another excellent idea is a 2-, maybe even a 3-year budget. This is such a massive entity. Certainly if we bring more things on budget, you need a little bit more time to thoughtfully appropriate and then really go back and audit and do those types of controls.

I did want to get to the tax gap just quickly. Do you have a basic breakdown of that \$385 billion tax gap? Where is it all coming from? Is it individual? Corporate?

Mr. DODARO. It is across the board. It is all the taxes, individual, corporate, estate taxes, payroll taxes.

Senator JOHNSON. Do you have a basic breakdown?

Mr. DODARO. The basic breakdown is that 84 percent of it comes from underreporting, and most of the underreporting is in individual income taxes, mostly for self-owned businesses, partnerships, and others. Most of the gap occurs in all taxes where there is not withholding at the income source. Generally speaking, where you have withholding at the income source, you do not have problems. But in these other areas, you do have problems. Ten percent of it comes from people who are properly assessed, but they just do not pay. And then about 6 percent of it is from people who do not file at all.

Senator JOHNSON. Okay. A last point, going back to the Department of Defense. You did talk about things like estimates of environmental liability, anti-deficiency, you talked about \$1 billion. Do you have some sort of sense of the close to \$600 billion defense budget, how much is actually accounted for and what percent really are some of these other issues that end up providing a qualified opinion?

Mr. DODARO. Very little. I mean, the military pensions can pass the test of an audit. They have in the past. Some of the smaller components, I think the Corps of Engineers and a couple others, offhand I would say it is less than 10 percent.

Senator JOHNSON. That is—

Mr. DODARO. That are passing an audit.

Senator JOHNSON. Okay, so, yeah, it is a massive problem.

Mr. DODARO. Yeah, it is a big problem. None of the major services have ever been able to pass an audit. So it is not anywhere near close to being solved.

Senator JOHNSON. Among many things, coming from the private sector, that I find unbelievable in Government, that certainly ranks right up there at the top. Like Senator Perdue was saying, if Wal-Mart can do it, why not the Department of Defense?

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Do either of you wish another chance here? Senator King.

Senator KING. Again, following up on the question about unpaid taxes, do you have any estimate of what it would cost to collect those unpaid taxes? In other words, for \$1 of additional enforcement or accounting or whatever in the IRS, what would we collect?

Mr. DODARO. Well, the IRS has estimates. I think it is \$5 for every \$1 put into an enforcement program. But, we think they could do a better job with the resources they currently have and how they allocate them. They do not really have good return on investment information about the different enforcement techniques that they have, like correspondence audits versus detailed audits. We have encouraged them to get better information.

But here are a number of things we have suggested where Congress could help. One is we think Congress ought to pass legislation to allow IRS to regulate paid tax preparers. A lot of people rely

on paid tax preparers. We found problems in limited studies that we have done, like we have sent undercover agents to 19 paid tax preparers. Only two gave us the right answer. And some of the other ones were so far off it would have cost, you know, penalties and interest. IRS data show that the paid tax preparers make errors in the earned income tax, which leads to some of the problems in improper payment in that program as well.

We think Congress could give IRS better math authority where they could match against administrative records and fix things right away without having to do an audit, without having to impose burdens.

Electronic filing could help as well. We suggest Congress lower the threshold of required businesses to provide information electronically to IRS. They could use third-party information a lot more effectively to match against the records to collect better tax information.

So we have a long list of—

Senator KING. If you could supply that list for the record, I would appreciate it.

Mr. DODARO. I will do that.

Senator KING. Thank you.

I think one of the points—and you have made this in your chart, again, going back to page 31, the alternative is health care. Most of that upward line is health care. And we can argue about who should pay it. In other words, should it be all Medicare? Or should it be partially? You know, there are all these proposals. But the bottom line is unless we deal with the underlying growth of the cost of health care, that is going to eat us up. It is going to eat up the whole rest of the budget. If you assume—if you see these numbers going up and you assume we cannot tolerate that level of debt, something is going to have to give, which is going to be the discretionary budget at the bottom end. We need to be thinking, as the largest consumer of health care in the country—I am sorry, not consumer but payor. We need to be thinking about how to get better value for the dollars that we are spending in terms of maybe more dollars for prevention and those kinds of things. But health care is the big driver here.

Mr. DODARO. No question about it. Health care, along with the demographics. The demographics are accentuating the—you know, on average now between 2029 and today, on average, over about 10,000 people in the United States turn 65 every day. And so that steady drumbeat of the retirement of the baby-boom generation, combined with health care costs, are really the key drivers, long-term health care, because eventually the demographics will even out.

Senator KING. I noted there were a couple of places in your testimony where you used the word “talent,” “insufficient talent.” And, again, it could well be a management problem of allocating talent and the personnel in the right and proper way. But in many cases, we do not have the people to do the necessary processing and work to adequately account or control expenditures or collect revenues.

Mr. DODARO. Right.

Senator KING. I think we shortchange this whole process by saying, well, we are going to reduce the size of the Federal Govern-



ment. But in reality, it is costing us money because we do not have the personnel to keep up with the demands.

Mr. DODARO. Yeah, I am very concerned about the Federal workforce. We have had it on our high-risk list since 2001. There are critical skill gaps in many different areas—finance, cybersecurity, acquisition. You know, we are not getting our dollars on procurement deals properly returned to us. And with the impending retirement of the baby-boom generation, I think it is going to make the skill gap even potentially more difficult.

Now, it presents a good opportunity if the agencies are ready to hire people with the necessary skills, because the need has changed over time.

Senator KING. Right.

Mr. DODARO. We have gone to using more contractors, but we have not adjusted to make sure we have the people that can manage and oversee the contractors. We are using more information technology, but we are not, you know, adjusted there as well. We have imposed requirements for financial audits but do not have the people—you know, a lot of people in the Defense Department have never been through a set of audited financial statements to know how to be able to do this.

So the workforce is a big concern to me, and I think you are going to see potential other Government breakdowns unless there is proper attention to this over the next 5 to 10 years in particular.

Senator KING. Thank you.

Thank you, Mr. Chairman.

Chairman ENZI. Senator Perdue.

Senator PERDUE. I just have one observation and one quick question. Thank you again for your forbearance today.

My experience with the system question goes back to the 1990s, and as a CEO, I have watched this for the last 20 years or so of my career, that with the explosive nature of the capability in the IT area, you get what you pay for, but at the same time, you can do a lot more than people think they can do with existing—and let me just give you an example.

I do not buy for a minute that we have not spent the money—or did not have the opportunity to spend the money inside the Federal Government to have world-class control systems. I am sorry, but I will give you one example. The State Department—and this is not a partisan comment because this goes back through three Presidencies. But if you look at the year 2000, we were spending about \$20 billion a year on State Department only, and that includes USAID, everything. The last few years, we are spending \$54 billion. Now, a lot of that increase happened during the Bush administration, so this is not a partisan comment about the current administration.

You cannot convince me that inside \$54 billion that organization could not have the absolute best, world-class IT systems available. It is not a priority. And that is a question of management throughout—across several Presidencies. That is just an observation.

Secondly, I would like to get your estimate right now what you think our net assets are in the Federal Government, just ballpark. I know they are not auditable. But what do you think the net assets are, all in?

Mr. DODARO. I think on the financial statements it is about—what is it, about \$3 trillion?

GAO STAFF. Net deficit is 20—

Mr. DODARO. Not the deficit. The assets.

Yeah, it is \$3 trillion, \$3.2 trillion.

Senator PERDUE. \$3 trillion.

Mr. DODARO. Right.

Senator PERDUE. And our net liabilities, if you were to take just the 30-year amortization of our future unfunded liabilities, what would that ballpark number be? I know Senator Johnson has done a good bit of work with, I think, CBO.

Mr. DODARO. Right.

Senator PERDUE. Maybe even GAO has got some estimates.

Mr. DODARO. Right. Well, the financial statements show, you know, \$21 trillion. We have many more liabilities than assets.

Senator PERDUE. No; I understand. But I am a little confused, because if you just look at the Social Security and Medicare liabilities over 30 years, it is much bigger than \$21 trillion.

Mr. DODARO. Yeah. There is a separate statement of social insurance in the financial statements. The amounts for Social Security and Medicare are not considered liabilities because the Congress can change those processes. But if you add everything—that is why we have the statement of social—you know, sustainability over time that shows that basically, you know, you have a huge gap, a fiscal gap.

Our simulations show that if you wanted to hold—this is the best way I know how to explain the magnitude of this issue. If you wanted to hold debt held by the public as a percent of gross domestic product at 74 percent, which it is now, which is much higher than the post-World War II—

Senator PERDUE. The problem is that what is held by the Government is growing faster than what is held by the public. And so I would argue that is kind of a moot point, that is a side—

Mr. DODARO. Well, no, but that—the intergovernmental trust funds are going down, intergovernmental holdings, because we are spending the money out of the Social Security Trust Fund to keep it going.

Senator PERDUE. I understand.

Mr. DODARO. But if you wanted to just hold that and stay at the debt held by the public that we are right now, you would have to increase revenues by 35 percent on average every year for the next 75 years or cut expenses by 26 percent under the current—

Senator PERDUE. Right. But this is my—and I will just submit this. I think the characterization that \$3 trillion in assets and \$21 trillion in liabilities is not the full picture based on what you just said, but I do not know whether the number is 100—I have seen numbers over \$100 trillion, \$125 trillion in terms of future unfunded liabilities, and I do not think many people would argue with that directionally being correct.

Mr. DODARO. Right.

Senator PERDUE. I would then argue that the assets are much bigger than \$3 trillion, if you look at what the United States Government actually owns—lands, resources, all that—and I have never seen an estimate of what that could be. And, honestly, I

think one of the things that is missing here is we talk about this from a cash accounting point of view and an income statement point of view, and not a balance sheet perspective in terms of dealing with debt. Debt to me has always been a balance sheet issue. You fund it and service it through your income statement, but you actually deal with it on the balance sheet.

So this goes back to today's whole hearing, and I thank you so much, Mr. Chairman. You know, I just think we have got to get a picture of this. So I would encourage us all to have a much more rigorous understanding of what our net assets are and what our—pick a year—30-year summary of total liabilities are so we can actually see whether we are insolvent or not. I mean, if it is 3 and 21, if that were the real number—which I do not think either one of those is right—it just highlights how serious this problem is.

Mr. DODARO. Yeah, well, if you look at the total set of financial statements in the audit, those are just the accrual base balance sheet. That is why we added the statement of sustainability over time.

Senator PERDUE. Right.

Mr. DODARO. There you get a clear picture that things are not sustainable over a period of time and what the magnitude of the fiscal gap is and the structural imbalance between revenues and expenditures.

Senator PERDUE. So if I were to bring you a public corporation that had assets of \$3 trillion in liabilities and 21, if those numbers were correct—which we have already agreed they are not. But if they were and you got an annual loss of revenue on your—or income, profit on your income statement, let us just take today's number of \$450 billion. And we know—the Senator is right—that these numbers are going up dramatically, projected. The CBO projects that we will add another \$9 to \$10 trillion to the Federal debt over the next 10 years. Would you argue that that is in a crisis situation?

Mr. DODARO. Yes. I have said it is unsustainable.

Senator PERDUE. I know.

Mr. DODARO. We are on a fiscal path that is unsustainable, and the sooner you take action, the better in terms of allowing people to adjust over time and adjustments to the economy over time. I mean, I think this is a very serious problem. I have said that for a number of years. And it will get more serious as time passes.

Senator PERDUE. So it is bigger than just the accounting issue, and I think you have called that out in this Committee before.

Mr. DODARO. Right.

Senator PERDUE. And I applaud you for doing that.

One last thing. You were the first agency, I think, to really get a handle on redundant agencies. A few years ago, you put this great report out. Senator Coburn took it and went to work on it, and I have not heard a lot of updates on that. But I remember the number being as high as somewhere between \$300 and \$400 billion of redundant agencies.

Has your agency, has the GAO had an update on that in the last year or two?

Mr. DODARO. Yes, we have had annual updates, and we are coming out next week with our sixth report.

Senator PERDUE. Okay. That was my question.

Mr. DODARO. That will be out next week.

Senator PERDUE. So what is the answer?

Mr. DODARO. The answer is so far enactment of our recommendations and our last update was about \$100 billion that has been saved so far or will be saved. But there is more on the table.

Senator PERDUE. No, I know. That is the question I am asking.

Mr. DODARO. Yeah.

Senator PERDUE. So good on you and good on the Federal Government to get \$100 billion out.

Mr. DODARO. Right.

Senator PERDUE. What is remaining?

Mr. DODARO. Well, there is tens of billions. I mean, it depends on what the Congress does. It is at a minimum an additional \$70 billion, and it could be more, likely more.

Senator PERDUE. Thank you.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you. I appreciate everybody's participation in this. I particularly want to thank Mr. Dodaro for his expert testimony. Of course, your full statement will be a part of the record, and we hope that you will be open to answering some written questions as well. The questions for the record would be due by 6:00 p.m. with a hard copy delivered to the Committee clerk in Dirksen 624, if anyone wants to do that.

I would note that one of the things that I have discovered as I have been going through this budget process is that the budget and the appropriations and the President's budget and Treasury's accounting all use different formats. And what I have also found out is that that is intentional. It makes it a little harder to follow the money. Somehow we have got to solve that. But I want to thank you for all of the suggestions that you included in your testimony. We will go through those as well.

Thank you, everybody, for your participation. If you have any suggestions on budget reforms, get them to me. We are going to have three more hearings this month yet, and then hopefully have some kind of a bill that we can hopefully get through in a bipartisan way. As I mentioned before, this is the time to do it, when nobody knows who the majority will be or who the President will be, so we can all be responsible.

Thank you. The meeting is adjourned.

[Whereupon, at 12:04 p.m., the Committee was adjourned.]

**Committee inserts for the April 6, 2016 hearing, titled Budgeting Blind: The Unreliability of Federal Financial Data, before the U.S. Senate Committee on the Budget.**

*From pages 43-44: Committee insert in reference to recommendations to be provided to the record on how the Federal Buildings fund could be used better in order to effectuate decisions*

*From GAO-14-239: Changes to the budgetary structure itself—within the bounds of the unified budget—might provide a more consistent way to meet real property needs while helping Congress and agencies make more prudent long-term fiscal decisions. Alternative budgetary structures should balance tradeoffs across two key GAO-identified budgeting and capital planning principles: (1) promoting transparency and fiscal control with regard to the funding of federal real property; and (2) providing agencies the flexibility to facilitate the acquisition, repair and alteration, and disposal of federal real property in support of federal missions.*

*GAO provides alternative budgetary structure options for Congress to consider. For example, in one option Congress would make the full balance of the Federal Buildings Fund available for funding real property projects, which could create room for additional agency flexibility but may reduce fiscal control. Another option would establish a government-wide capital acquisition fund with authority to borrow from the Federal Financing Bank for approved projects, which could improve transparency of both costs and benefits upfront and over time while business case analyses could provide a means of assuring fiscal control.*

*From page 45: Committee insert in response to Senator King's request regarding GDP growth assumptions for GAO's simulation*

*The average growth rate in real GDP for GAO's simulation period (2015-2089) is 2.1 percent.*

*From pages 65-66: Committee insert in response to Senator King's request to supply a list of GAO recommendations to IRS and Congress to help collect unpaid taxes. (see attached pages below)*

### Open GAO Recommendations to Address the Tax Gap

GAO has made numerous recommendations to Congress and the Internal Revenue Service (IRS) to improve tax compliance and reduce the tax gap, many of which have been implemented and have resulted in billions of dollars of additional revenue. Below are some key recommendations that have yet to be implemented, along with information on the specific tax compliance issues they seek to address. The status of these recommendations can be found at [www.gao.gov](http://www.gao.gov) by searching for the report number listed (in parenthesis) with the recommendation.

Tax compliance issue	Matter for Congressional consideration (MC) or recommendation to IRS (Rec)
<b>Math Error Authority</b>	
IRS does not have broad statutory authority to correct certain "math errors," such as calculation mistakes or omitted or inconsistent entries, during tax return processing (or for specific compliance issues)	<ul style="list-style-type: none"> <li>• MC: Consider granting IRS specific math error authority to use prior years' tax return information to ensure that taxpayers do not improperly claim credits or deductions in excess of lifetime limits, where applicable (GAO-11-481)</li> <li>• MC: Consider granting IRS broader math error authority, with appropriate safeguards against misuse of that authority, to correct errors during tax return processing (GAO-10-349)</li> <li>• MC: Consider granting IRS specific math error authority to use prior year tax return information to automatically verify taxpayers' compliance with the number of years the Hope credit can be claimed (GAO-10-225)</li> <li>• MC: Consider granting IRS specific math error authority to identify and correct returns with ineligible IRA catch-up contributions and contributions to traditional IRAs from taxpayers older than 70 ½ (GAO-09-146)</li> <li>• Rec: Assess whether data received from health insurance marketplaces are sufficiently complete and accurate to enable effective correction of health insurance information—including the premium tax credit—on tax returns at-filing; seek legislative authority to correct tax returns at-filing if data are sufficiently complete and accurate (GAO-15-540)</li> <li>• Note: the 2016 Consolidated Appropriations Act provided IRS with additional math error authority to deny certain refundable tax credits claimed by taxpayers who previously fraudulently or improperly claimed such credits.</li> </ul>
<b>Paid tax return preparers</b>	
Some paid tax return preparers make significant errors in preparing tax returns	<ul style="list-style-type: none"> <li>• MC: Consider requiring unenrolled preparers (e.g., those other than CPAs or enrolled agents) to complete testing and continuing education requirements (GAO-14-467T)</li> </ul>
<b>Information reporting</b>	
Some sources of income are not subject to third-party information reporting, a tool that has been shown to improve tax compliance	<ul style="list-style-type: none"> <li>• MC: Consider requiring information reporting to IRS of (1) certain service payments (e.g., repairs) made by taxpayers who rent out real estate (GAO-08-956) and (2) service payments made to corporations (GAO-09-238)</li> </ul>
Incomplete and delayed data from health insurance marketplaces limited IRS's ability to match taxpayer Premium Tax Credit (PTC) claims to marketplace data at the time of tax return filing	<ul style="list-style-type: none"> <li>• Rec: Assess whether the challenges in getting complete and accurate marketplace data in time to conduct pre-refund verification of taxpayer premium tax credit claims are a single year or an ongoing problem and, if they are an ongoing problem, assess the effects of the problem and options for correcting it (GAO-15-540)</li> </ul>

Tax compliance issue	Matter for Congressional Consideration (MC) or Recommendation to IRS (Rec)
<b>Information reporting (cont.)</b>	
Mortgage-secured property addresses must be reported on the 1098 mortgage interest statement, but not on forms used to collect information about cancelled mortgage debt	<ul style="list-style-type: none"> <li>Rec: Require mortgage-secured property addresses to be reported on other forms (Forms 982 and 1099-C) to help IRS detect taxpayers who fail to pay taxes on certain forgiven mortgage debts (GAO-10-997)</li> </ul>
<b>Partnerships and S corporations</b>	
Paper-filed corporate and partnership tax returns limit IRS's ability to use data in a comprehensive, resource-efficient way	<ul style="list-style-type: none"> <li>MC: Consider expanding the electronic tax return filing mandate for partnerships and corporations (GAO-14-453)</li> </ul>
IRS has limited information about the extent and nature of income misreporting by partnerships, as well as about the effectiveness of its examinations in detecting such misreporting	<ul style="list-style-type: none"> <li>Rec: Improve enforcement data for partnerships by (1) developing a strategy to better estimate the extent and nature of partnership misreporting and the effectiveness of partnership examinations (GAO-14-453), and (2) tracking and analyzing the results of large partnership examinations (GAO-14-732)</li> </ul>
IRS does not match information returns on income from partnerships and S corporations to tax returns from partners and shareholders that are themselves partnerships and S corporations	<ul style="list-style-type: none"> <li>Rec: Test the feasibility of matching the K-1 information return—on which partnerships and S corporations report income distributed to partners or shareholders—to income information on tax returns for partners and shareholders that are themselves partnerships and S corporations (GAO-14-453)</li> </ul>
Some shareholders of S corporations make mistakes in calculating basis—their ownership share of the corporation—when taking losses passed through to them from the corporation, potentially decreasing their total taxes	<ul style="list-style-type: none"> <li>MC: Consider requiring S corporations to use information already available to them to calculate shareholders' basis as completely as possible and report it to shareholders and IRS (GAO-10-195)</li> </ul>
<b>Business tax compliance</b>	
Some Medicaid providers have unpaid federal taxes	<ul style="list-style-type: none"> <li>Rec: Explore further opportunities to enhance the collection of unpaid federal taxes from Medicaid providers, including a cost-benefit analysis of the implementation of a continuous levy program and expanded use of levies against providers with large Medicaid payments and significant unpaid federal taxes, where appropriate, seek legislation to modify existing law to allow for more efficient collection of outstanding tax debts from Medicaid providers (GAO-11-493)</li> </ul>
IRS does not have an agency-wide approach for addressing tax evasion among the at least one million networks of businesses and related entities	<ul style="list-style-type: none"> <li>Rec: Create an agency-wide strategy with goals to coordinate and plan its enforcement efforts on network tax evasion (GAO-10-968)</li> </ul>

Tax compliance issue	Matter for Congressional Consideration (MC) or Recommendation to IRS (Rec)
<b>Business tax compliance (cont.)</b>	
IRS does not know how many businesses failed to file required returns (nonfilers); many nonfiler cases it investigates are unproductive because the business does not need to file the return IRS expects	<ul style="list-style-type: none"> <li>Rec: Develop at least a partial estimate for the business nonfiler rate based on IRS's existing inventory of cases and set a deadline for developing performance data on business nonfiler efforts (GAO-10-950)</li> </ul>
Tax noncompliance by sole proprietors accounts for a large share of the tax gap	<ul style="list-style-type: none"> <li>Rec: Use ongoing research efforts to develop a better understanding of the nature of sole proprietor noncompliance, including sole proprietors improperly claiming business losses (GAO-09-815)</li> </ul>
	<ul style="list-style-type: none"> <li>Rec (to Treasury): Ensure that the strategy to address the tax gap covers sole proprietor compliance in detail while coordinating it with broader tax gap reduction efforts (GAO-07-1014)</li> </ul>
<b>Individual retirement accounts (IRA)</b>	
IRA owners investing in hard-to-value non-publicly traded assets can escape taxation on investment gains and face greater risk of engaging in prohibited transactions	<ul style="list-style-type: none"> <li>Rec: Approve plans to fully compile and digitize the new data from electronic and paper-filed Forms 5498 to ensure the efficient use of the information on non-publicly traded IRA assets (GAO-15-16)</li> </ul>
	<ul style="list-style-type: none"> <li>Rec: Conduct research using the new Form 5498 data to IRAs holding nonpublic asset types and use that information for an IRS-wide strategy to target enforcement efforts and provide outreach targeting taxpayers with nonpublic IRA assets and their custodians (GAO-15-16)</li> </ul>
	<ul style="list-style-type: none"> <li>Rec: Build on research data regarding IRAs holding nonpublic assets, and identify options to provide outreach targeting taxpayers with nonpublic IRA assets and their custodians, such as reminder notices that engaging in prohibited transactions can result in loss of the IRA's tax-favored status (GAO-15-16)</li> </ul>
	<ul style="list-style-type: none"> <li>Rec: Work in consultation with the Department of the Treasury on a legislative proposal to expand the statute of limitations on IRA noncompliance to help IRS pursue valuation-related misreporting and prohibited transactions that may have originated outside the current statute's 3-year window (GAO-15-16)</li> </ul>



Tax compliance issue	Matter for Congressional Consideration (MC) or Recommendation to IRS (Rec)
IRS resources and administration	
IRS does not have an evaluation plan for the payment card pilot program it developed to test ways 3 <sup>rd</sup> party credit card and similar payment information can be used to address taxpayer noncompliance	<ul style="list-style-type: none"> <li>Rec: Clearly define the stages of the pilot and establish measurable goals for determining when the pilot progresses from one stage to the next and develop an evaluation plan for the overall pilot that includes evaluation questions, complete descriptions of needed data, and evaluation criteria (GAO-15-513)</li> </ul>
IRS's declining budget environment and increased workload demands create challenges in allocating resources	<ul style="list-style-type: none"> <li>Rec: Develop a long-term strategy to address operations amidst an uncertain budget environment (GAO-14-605)</li> <li>Rec: Make better use of return on investment data, for example, by reviewing disparities in the ratios of direct revenue yield to costs across different enforcement programs and across different groups of cases within programs, and by determining whether this evidence provides a basis for adjusting the allocation of annual enforcement resources (GAO-13-151)</li> </ul>
IRS does not have information to determine how its program of examining tax returns via correspondence affects the agency's broader strategic goals for compliance, taxpayer burden, and cost	<ul style="list-style-type: none"> <li>Rec: Establish formal objectives for the correspondence audit program, ensure that program measures reflect those objectives, and clearly link those measures with strategic IRS-wide goals for ensuring compliance in a cost-effective way while minimizing taxpayer burden (GAO-14-479)</li> </ul>
Limited risk-based approaches to collecting taxpayer debt may lead to delayed collection of debt, higher costs for IRS, and additional penalties for taxpayers who pay late.	<ul style="list-style-type: none"> <li>Rec: Pilot more risk-based approaches for contacting taxpayers who have a balance due, which could include implementing its data analytics plan (GAO-13-156)</li> </ul>
No quantitative measure of scope for major IT investments to determine delivered functionality	<ul style="list-style-type: none"> <li>Rec: Develop a quantitative measure of scope (a measure of whether an investment delivered the functionality that was paid for), at a minimum, for its major information technology investments to have information on the performance of these investments (GAO-12-603)</li> </ul>
IRS has not explored several low-cost and easy-to-implement options that could help it clarify how to treat forgiven mortgage debt for tax purposes	<ul style="list-style-type: none"> <li>Rec: Determine how refocusing mortgage debt enforcement efforts could gain additional revenue by taking some relatively low-cost steps, including revising the associated forms; collecting more information from taxpayers and lenders; and using third-party data to determine whether taxpayers are correctly excluding forgiven mortgage debt from taxable income (GAO-10-997)</li> </ul>

Tax compliance issue	Matter for Congressional Consideration (MC) or Recommendation to IRS (Rec)
IRS resources and administration (cont.)	
Examinations of real-estate tax deductions include little focus on whether taxpayers claimed non-deductible items: IRS guidance does not require examiners to request proof of deductibility or direct them to look for nondeductible charges on tax bills	<ul style="list-style-type: none"> <li>Rec: Clarify in examination guidance the type of evidence for verifying deductibility and require examiners to ask taxpayers to substantiate deductions that appear to include nondeductible charges that are large, unusual, or questionable (GAO-09-521)</li> </ul>
IRS referral and whistleblower programs	
IRS does not have a formal mechanism to facilitate information sharing across nine referral programs, including a largely manual processes forcing IRS to spend resources reading and routing the referrals	<ul style="list-style-type: none"> <li>Rec: Establish a coordination mechanism to facilitate communication and information sharing across IRS referral programs on crosscutting tax issues and ways to improve efficiency in the mechanisms for public reporting of possible tax violations (GAO-16-155)</li> <li>Rec: Coordinate on a plan and timeline for developing a consolidated, online referral submission in order to better position IRS to leverage specialized expertise while exploring options to further consolidate initial referral screening operations (GAO-16-155)</li> </ul>
IRS does not have an organizational structure for defining objectives and outcomes for the information referral process and has ineffective controls over screening and routing information referrals for further action	<ul style="list-style-type: none"> <li>Rec: Establish, document, and implement an organizational structure identifying responsibility for defining objectives with an appropriate line of reporting for measuring costs and results for information referrals (GAO-16-155)</li> <li>Rec: Ensure that the Internal Revenue Manual has internal controls for processing information referrals by establishing, documenting, and implementing procedures for screening and routing information referrals as well as monitoring referrals retained for destruction and misroute errors (GAO-16-155)</li> </ul>
Tax whistleblowers do not have statutory protections against retaliation from employers; which may discourage whistleblowers from coming forward	<ul style="list-style-type: none"> <li>MC: Consider legislation that would provide protections for tax whistleblowers against retaliation from their employers (GAO-16-20)</li> </ul>
Delayed processing and a lack of communications discourage whistleblowers from coming forward	<ul style="list-style-type: none"> <li>Rec: Implement a staffing plan for streamlining the intake and initial review process for the whistleblower program to make more efficient use of staff resources (GAO-16-20)</li> <li>Rec: Develop an additional or revised fact sheet about the whistleblower program, or publish additional information the program on the IRS website, or both (GAO-16-20)</li> </ul>
IRS has not collected comprehensive information to evaluate whether the benefit of a recent pilot program to send letters to whistleblowers annually was worth the costs	<ul style="list-style-type: none"> <li>Rec: Develop a comprehensive plan for evaluating the costs and benefits of the pilot annual status letter program, including obtaining feedback from whistleblowers in the pilot regarding the usefulness of the letter (GAO-16-20)</li> </ul>

Tax compliance issue IRS taxpayer service	Matter for Congressional Consideration (MC) or Recommendation to IRS (Rec)
<p>IRS's declining budget environment and increased workload demands demonstrate the need to better leverage automated processes</p>	<ul style="list-style-type: none"> <li>Rec: Develop a long-term strategy to improve web services provided to taxpayers, including business cases that describe potential benefits and costs, which are used to prioritize future projects (GAO-13-435)</li> <li>Rec: Finalize a more comprehensive plan for online services, including an assessment of granting taxpayers the ability to update their account information online (GAO-12-176)</li> </ul>
<p>IRS struggles in providing telephone service to taxpayers in the midst of declining resources, increasing statutory responsibilities, and growing demand from taxpayers</p>	<ul style="list-style-type: none"> <li>Rec: Systematically and periodically compare its telephone service to the best in business to identify gaps between actual and desired performance; determine a customer service telephone standard and the resources required to achieve this standard based on input from Congress and other stakeholders (GAO-15-163)</li> <li>Rec: Develop a strategy that defines appropriate levels of telephone and correspondence service and wait time and lists specific steps to manage service based on an assessment of time frames, demand, capabilities, and resources (GAO-13-156)</li> </ul>
<p><b>Identity Theft Related Refund Fraud</b></p>	
<p>IRS's efforts to centralize taxpayer authentication across its systems do not include cost, benefit, and risk analyses, which would help inform IRS's and Congress's decisions about whether and how much to invest in the various authentication options</p>	<ul style="list-style-type: none"> <li>Rec: Estimate and document the costs, benefits, and risks of possible options for taxpayer authentication (GAO-15-119)</li> </ul>
<p>Reducing the e-file threshold for Form W-2 (filers with fewer than 250 information returns annually can file paper Forms W-2) would allow IRS to obtain timely, accurate data from a significant number of employers and would enhance the benefits IRS could obtain from an accelerated W-2 deadline and pre-refund W-2 matching</p>	<ul style="list-style-type: none"> <li>MC: Consider granting Treasury the authority to lower the threshold for electronic filing of Forms W-2 to help combat identity theft related refund fraud through earlier, pre-fund matching of W-2s to tax returns (GAO-14-633)</li> </ul>



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U.S. GOVERNMENT ACCOUNTABILITY OFFICE

Comptroller General  
of the United States

**Questions for the Record**

**From Chairman Enzi**

**For the Honorable Gene Dodaro**

***"Budgeting Blind: The Unreliability of Federal Financial Data"***

**April 6, 2016**

**Senate Budget Committee**

**Question #1:**

The financial statements of the federal government that GAO audited are compiled on an accrual, or "modified cash," basis. As such, they display financial information differently than does the primarily cash budget with which Congress typically works. As a result, the federal deficit does not directly equate with the "net operating loss" as recorded in the financial statements. And certain items included as liabilities in the financial statements - earned veterans' benefits and federal employee retirement benefits, for instance -- are not treated as such under the primarily cash budget.

**As Federal lawmakers, we work with a primarily cash budget. How are the accrual-based financial statements different, and what can we learn from them?**

Together the financial statements and the federal budget provide a more complete picture of the federal government's fiscal and financial condition than either alone provides. There is very little difference between how accrual measures (in the financial statements) and cash measures (in the budget) record revenue, because the financial statements primarily record revenue on a modified cash basis. The differences arise almost entirely on the spending side with the timing of when costs for some activities are recognized.<sup>1</sup> Accrual-based financial statements recognize costs when the goods are used. The primarily cash budget recognizes costs when the payment is made for the goods. As discussed below, differences arise when a cost is accrued in one fiscal year but paid for in another fiscal year, as is the case with federal civilian and military retirement benefits. For some areas, such as federal civilian and military employee salaries,

<sup>1</sup>See GAO, *Budget Issues: Accrual Budgeting Useful in Certain Areas but Does Not Provide Sufficient Information for Reporting on Our Nation's Longer-Term Fiscal Challenge*, GAO-08-206 (Washington, D.C.: Dec. 20, 2007); and GAO, *Fiscal Outlook: Measuring the Federal Deficit* (2016), accessed April 1, 2016, [http://www.gao.gov/fiscal\\_outlook/measuring\\_the\\_federal\\_deficit/overview](http://www.gao.gov/fiscal_outlook/measuring_the_federal_deficit/overview).

there is little difference between accrual and budget measures because the time between the underlying event (e.g., work performed, wages earned) and the payment is relatively short. Neither accrual nor budget measures include future benefits for social insurance and other entitlement programs.

**In measuring the federal deficit, how does the size of the reported accrual deficit compare with the size of the regular cash-based budget deficit to which we typically refer? What factors primarily account for the difference?**

As reported in the *2015 Financial Report*, the federal government's reported "bottom line" accrual net operating cost for fiscal year 2015 of \$520 billion was \$81 billion higher than the reported budget deficit of \$440 billion. The excess of the accrual net operating cost over the budget deficit is primarily due to costs incurred but not paid associated with increases in estimated federal employee and veteran benefits liabilities and certain other liabilities that are included in net operating cost, but not the budget deficit. The reasons for differences between the budget and accrual measures vary by program area. For program areas such as federal employee and veteran benefits, we have found that the key difference between the accrual and cash measures is the annual change in the liability, which is generally equal to accrued expenses less cash payments made to reduce the liability.<sup>2</sup>

While capital assets and financial assets and liabilities are also treated differently in the cash and accrual deficits, the reasons are unique to those program areas.

- **Capital assets:** When capital assets, such as structures and equipment, are purchased, the budget records an obligation for the full cost up front in order to provide decision makers with the information and incentives to make efficient decisions at the only time that they can control the cost. Outlays are recorded when a capital asset is paid for and therefore increases the cash deficit in the year that the outlay is made. However, the accrual deficit only reflects one year's worth of cost, called depreciation expense. Under the accrual basis of accounting used in the financial statements, the cost of the asset is initially recorded on the balance sheet and is then spread over its expected useful life to match the asset's cost with its use.

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<sup>2</sup>GAO, *Fiscal Outlook: Measuring the Federal Deficit* (2016), accessed April 1, 2016, [http://www.gao.gov/fiscal\\_outlook/measuring\\_the\\_federal\\_deficit/overview](http://www.gao.gov/fiscal_outlook/measuring_the_federal_deficit/overview).

- **Financial assets and liabilities:** Financial assets and liabilities include loans and loan guarantees that have generally been recorded similarly in the budget and the financial statements—the net present value of the estimated cost is recorded when the transaction occurs. However changes in the estimated cost of loans and loan guarantees are reflected at different times. The re-estimated costs are reflected in the accrual deficit at fiscal year-end but are not reflected in the cash deficit until the following fiscal year.

**Question #2:**

According to your testimony, the Defense Department's inauditability is a major reason the government-wide financial statements are inauditable each year. Defense is the federal government's largest department, representing about 30 percent of the federal government's reported total assets as of September 30, 2015, and approximately 15 percent of the federal government's reported net cost for fiscal year 2015.

The National Defense Authorization Act (NDAA) for Fiscal Year 2010 requires that DOD's Financial Improvement and Audit Readiness (FIAR) Plan set as its goal that the department's financial statements be validated as ready for audit by September 30, 2017.

**Can you describe the status of the Department of Defense's progress toward producing auditable financial statements? Do you think it will meet the current goal of preparing auditable statements for Fiscal Year 2017?**

The Department of Defense (DOD) has self-identified seven critical areas that need to be resolved in order to meet its goal of auditable department-wide financial statements by September 30, 2017, including

- Ensuring that the universe of transactions (i.e., the entirety of underlying accounting transactions) reconcile to the general ledger and ultimately financial statement line items.
- Reconciling DOD's fund balance with Treasury.

- Providing support for journal vouchers that are adjusting entries being made to correct unreconciled differences.
- Providing support for the existence and completeness of assets.
- Establishing property and asset values.
- Establishing controls for producing an auditable cost estimate for DOD's environmental liabilities.
- Providing support for open obligations (i.e., delivered and undelivered orders) for which payment has not yet been made.

As the pilot military service, the Marine Corps underwent its first Schedule of Budgetary Activity audit for fiscal year 2012. However, the Marine Corps' fiscal year 2012 audit report was rescinded, its fiscal year 2013 audit report was not issued, and the Marine Corps received a disclaimer on its fiscal year 2014 Schedule of Budgetary Activity. The audit contract with an Independent Public Accounting (IPA) firm for the Marine Corps' fiscal year 2015 Schedule of Budgetary Activity was cancelled in March 2016 before audit work was completed.

The military services (i.e. Army, Navy, and Air Force) asserted audit readiness for their Schedules of Budgetary Activity during fiscal year 2014 and underwent their first-year Schedule of Budgetary Activity audits during fiscal year 2015. The IPAs issued disclaimers of opinion on the fiscal year 2015 Schedules of Budgetary Activity, and identified material weaknesses in internal control at all three military services. Army, Navy, and Air Force management have generally concurred with the findings in the respective IPA reports and stated that they will develop and execute corrective actions to address the IPAs' recommendations. In its November 2015 FIAR Plan Status Report, DOD reported that the Army, the Navy, and the Air Force will again undergo Schedule of Budgetary Activity audits for fiscal year 2016. The disclaimers of opinion are a result of long-standing, uncorrected weaknesses in financial management processes, systems and controls.

In addition, we agree with the DOD Office of Inspector General's (OIG), assessment, that meeting the September 2017 deadline for audit ready financial statements remains a significant challenge, as the department also must focus on integration of service provider processes,

achieving an audit ready systems environment for its legacy and Enterprise Resource Planning (ERP) systems, and attracting and retaining qualified financial management personnel.

**Are there unique challenges does the Defense Department face in achieving auditability? If so, please describe them.**

DOD is one of the largest and most complex organizations in the world. Its operations span a wide range of organizations, including the military services and their respective major commands and functional activities, agencies and field activities, and combatant and joint operational commands responsible for military operations.

The greatest obstacles currently preventing DOD from achieving its audit readiness goals include, (1) the lack of qualified and experienced financial management personnel, (2) business systems that meet financial management accounting requirements, and (3) long-standing material internal control weaknesses.

As it relates to DOD's financial management workforce, we have reported that DOD has not met statutory requirements for assessing the gap between existing and future critical-skills needs. Also, there is a need for qualified and experienced personnel—not only at working levels, but also in senior leadership positions. In addition, DOD's automated financial management and related business systems do not adequately support material amounts in DOD's financial statements. Further, DOD will need to address its long-standing material weaknesses, such as its inability to accurately account for its assets, deficiencies in financial management systems, and funds control weaknesses, in order to implement lasting financial management reform.

**According to your written testimony, "DOD faces challenges in its efforts to provide reasonable assurance of accountability for its property, plant, and equipment-knowing what it has, where it is located, what condition it is in, and what it cost." Considering this current state of affairs - and similar problems GAO has chronicled recently concerning the federal civilian real property inventory - are there practical obstacles to Congress implementing a capital budget at this point in time?**

The current data available on the government's federal real property assets does not facilitate wise investment in federal real property or implementing a capital budget. Since 2003, federal real property management has been on our High-Risk List given long-standing challenges in the federal government managing its real property. In our 2015 update to the High-Risk List, we



reported that since 2003, the government has given high-level attention to this issue and has made strides in real property management, but continues to face challenges.<sup>3</sup> For example, the federal government continues to maintain too much excess and underutilized property. It also relies too heavily on leasing in situations where ownership would be more cost efficient in the long run. In addition, the federal government faces ongoing challenges in protecting its facilities. Finally, effective real property management and reform are undermined by unreliable real property data.

Despite a high level of leadership commitment to improve real property data, the federal government continues to face challenges with the accuracy and consistency of the Federal Real Property Profile (FRPP)—an inventory to track federal real property government wide—causing the federal government to report inaccurate inventory and outcome information, thereby limiting its usefulness for supporting sound decision making. These flaws have implications—for instance, we found that the \$3.8 billion reported by agencies in 2012 as cost savings from real property disposal, space management, sustainability, and innovation activities was not reliable—cost savings were based on different assumptions, methodologies, and timelines that reduced the reliability of the data. GSA took steps to improve the reliability of FRPP data, but these changes have not yet sufficiently improved the overall reliability of the data and the federal government continues to lack an action plan for making additional improvements.

We support building an investment component into the federal unified budget structure. While the federal unified budget does not separate capital from operating budgets, it focuses policymakers' attention on the effect of federal cash borrowing on the economy. Such a focus is critical to understand how federal budgetary decisions in the aggregate affect the business cycle in the short term as well as potential consequences for longer-term economic output. We recognize that the federal unified budget does not highlight the different effects that various types of spending would have on the long-term potential output of the economy. Accordingly, GAO has suggested that using an investment component, within the context of the unified budget, could help Congress make better informed decisions about federal spending on consumption versus investments intended to foster economic growth.

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<sup>3</sup>GAO, *High-Risk Series: An Update*, GAO-15-290 (Washington, D.C.: Feb. 11, 2015).

In discussing federal budgeting for capital, it is important to remember the federal government's unique role in the economy. It is useful to look at the federal government in two different ways: it is both a partial custodian of the economic health of the nation and an operating entity.

- As a **partial custodian** of the nation's economy, the government invests in activities that are intended to increase the private sector's long-term productivity and growth, such as education, research and development, and infrastructure. For the most part, the federal government provides its support for investment through federal subsidies to other levels of government or the private sector. While providing long-term benefits to the nation as a whole, much of this spending does not result in assets owned by the federal government.
- As an **operating entity**, the federal government makes expenditures on physical assets, such as federal office buildings and hospitals, land, major equipment, and information technology that provide long-term benefits to the government's own operations.

**Question #3:**

GAO has reported information security as a high-risk area across government since February 1997. During the recent government-wide audit, GAO found that, *"serious and widespread information security control deficiencies continued to place federal assets at risk of inadvertent or deliberate misuse, financial information at risk of unauthorized modification or destruction, sensitive information at risk of inappropriate disclosure, and critical operations at risk of disruption."*

As you know, federal agencies have experienced several significant breaches of federal data. These have involved unauthorized release of federal employee and federal contract employee data, as well as security clearance data.

**Please describe the extent to which federal data security deficiencies are attributable to each of the following factors:**

- 1. Poor management and procedures;**
- 2. Insufficient personnel with necessary skills and experience; and**

### **3. Inadequate or outdated information technology architecture**

Federal data security deficiencies can be attributed to among other things, insufficient programs and procedures, shortages of skilled IT staff, and outdated IT architecture. We have previously reported<sup>4</sup> that an underlying cause for information security weaknesses identified at federal agencies was that agencies had not fully implemented their information security programs. These programs are required by the Federal Information Security Modernization Act of 2014,<sup>5</sup> which provides a framework for assessing and managing risk, including developing and implementing security policies and procedures.

In addition, as we reported in our 2015 High-Risk update,<sup>6</sup> skill gaps were a contributing factor for information security continuing to be a government-wide high risk area. In that report, we indicated that steps had been taken to close critical skills gaps in the cybersecurity area, but that it remains an ongoing problem and additional efforts are needed to address the issue.

Finally, inadequate IT architecture also contributes to security deficiencies since older systems often lack key controls and may be vulnerable. For example, we and inspectors general often identify weaknesses with outdated software, where such software is no longer supported by the vendor.

#### **Your testimony states that federal financial information is at risk of unauthorized modification or destruction. How do you recommend we further safeguard this information in the short-term, and over the long-run?**

To further safeguard information and systems in both the short term and over the long run, agencies need to fully and effectively implement agency-wide information security programs that manage risk on an ongoing basis. In addition, agencies need to 1) strengthen controls intended to prevent, detect, and restrict unauthorized or improper access to systems and information; 2) securely configure network and system devices to mitigate known vulnerabilities; 3) appropriately separate incompatible duties among users; 4) implement GAO and inspector

<sup>4</sup>GAO, Federal Information Security: *Agencies Need to Correct Weaknesses and Fully Implement Security Programs*, GAO-15-714 (Washington, D.C.: Sept. 29, 2015).

<sup>5</sup>The Federal Information Security Modernization Act of 2014 (FISMA 2014), among other things, requires the head of each agency to provide information security protections commensurate with the risk and magnitude of harm resulting from unauthorized access, use, disclosure, disruption, modification, or destruction of the agency's information or information systems. Pub. L. No. 113-283, § 2(a), 128 Stat. 3073 (Dec. 18, 2014), codified at 44 U.S.C. § 3554(a).

<sup>6</sup>GAO, High-Risk Series: *An Update*, GAO-15-290 (Washington, D.C.: Feb. 11, 2015).

general recommendations, which can assist them with strengthening the security over their information and systems;<sup>7</sup> 5) implement continuous diagnostics and mitigation (CDM) activities; and 6) bolster intrusion detection, prevention, and response capabilities.

**Question #4:**

GAO's written testimony describes how the government has made strides forward in financial management, but still faces considerable challenges. Almost all of the 24 major federal agencies produced auditable financial statements for fiscal year 2015, for instance, whereas only six agencies did so in 1996. But major problems still exist, ranging from the inability to reconcile intragovernmental accounts to insufficient data security.

The Federal Financial Management Improvement Act of 1996 (FFMIA) was designed to lead to system improvements that would result in agency managers routinely having access to reliable, useful, and timely financial-related information with which to measure performance and increase accountability. For fiscal year 2015, auditors at 12 of the 24 CFO Act agencies reported that the agencies' financial management systems did not substantially comply with one or more of the three FFMIA requirements.

**How do the financial management practices of the federal government compare with the state of the art in the private sector?**

Like public traded private sector entities, federal entities are required to prepare financial statements and have them audited. Federally required statements present similar information, with the governmentwide statements providing the sustainability information we have discussed.

As referenced in our testimony statement, the challenges that we see in federal financial management include

- Material weaknesses in internal control
- Inadequate financial management systems

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<sup>7</sup>GAO-15-714; GAO, Information Security: *Department of Education and Other Federal Agencies Need to Better Implement Controls*, GAO-16-22T (Washington, D.C.: Nov. 17, 2015); GAO, Information Security: *Federal Agencies Need to Better Protect Sensitive Data*, GAO-16-194T (Washington, D.C.: Nov. 17, 2015).

- Lack of reliable, useful, and timely information for management decision-making

**How do the information security protections surrounding federal data compare with the state of the art practices in the private sector?**

Although limited, our work has shown that the private sector uses similar security protections and suffers from the same types of vulnerabilities as the federal government. The National Institute of Standards and Technology has developed a robust body of information security guidance that is comparable to that in the private sector. Like the federal government, private sector organizations have experienced devastating security attacks.

**What accounts for the state of financial management in the federal government as compared to the private sector?**

Incentives for reliable, useful, and timely information in the private sector are driven by competition and the need to raise capital. The users of private sector financial statements include investors and regulators, who will not react positively to material weaknesses in internal control and/or disclaimers of opinions. Such incentives may not exist to the same degree in the government. For example, the lack of reliable, useful and timely information has not had an apparent significant impact on the federal government's ability to raise capital through borrowing.

**How accountable do you think federal managers feel for their financial management practices? Do they feel more, less or equally accountable for their financial management as compared with their counterparts in publicly-held companies in the private sector that are subject to e.g. SEC financial reporting requirements?**

GAO has not conducted work to determine the extent to which federal managers feel accountable for their financial management practices when compared to their counterparts in publicly-held companies. However, one way to judge accountability is to consider the significant progress agencies have made since the enactment of key federal financial management reforms in the 1990s in improving federal financial management activities and practices. For fiscal year 2015, almost all of the 24 CFO Act agencies received unmodified ("clean") audit opinions on their respective entities' financial statements, up from 6 CFO Act agencies for fiscal year 1996. In addition, accounting and financial reporting standards have continued to evolve to provide greater transparency and accountability over the federal government's operations, financial condition, and fiscal outlook.

**Question #5:**

In fiscal year 2015, agencies reported improper payment estimates totaling \$136.7 billion, a significant increase-over \$12 billion, mainly due to an increased error rate in Medicaid-from the prior year's revised estimate of \$124.6 billion. The estimated government wide error rate increased from fiscal year 2014 to fiscal year 2015 (from 4.5 percent of program outlays to 4.8 percent).

The estimated improper payments for fiscal year 2015 were attributable to 121 programs spread among 22 agencies. While these 121 programs span various agencies across the federal government, improper payment estimates for Medicare, Medicaid, and the Earned Income Tax Credit accounted for more than 76 percent of the government wide estimate.

Your audit report mentions that some federal entities failed to report improper payment rates for certain risk-susceptible programs, and you stated during the hearing that the reported total of \$136.7 billion in improper payments last year likely underestimates the problem.

**How much greater might the overall total of improper payments be if all federal entities with risk-susceptible programs were to report as required?**

It is not currently possible to determine reliably the extent to which the government-wide improper payment is understated. Unless and until all risk assessments are determined to be reliable, all risk-susceptible programs prepare estimates of improper payments, and all estimating methodologies are found to be reasonable, the total amount of improper payments cannot be determined. The following are examples of these issues.

- In fiscal year 2015, three agencies did not report improper payment estimates for five risk-susceptible programs, most significantly HHS's Temporary Assistance for Needy Families (TANF) program with outlays of more than \$16 billion.
- Further, DOD's fiscal year 2015 improper payment estimates may not be reliable because the DOD IG reported that the agency could not reconcile outlays to ensure that all relevant payments were captured for review.
- Prior GAO work has shown that certain estimates may be understated. For example, DOD does not review medical necessity when estimating TRICARE improper payments. CMS reports that a significant portion of its improper payments relate to medical necessity for Medicare Fee-for-Service, a program similar to DOD's TRICARE.

- Finally, various IGs also reported deficiencies related to compliance with criteria listed in the Improper Payments Elimination and Recovery Act for fiscal year 2014, including risk-susceptible programs that did not report improper payment estimates, estimation methodologies that may not produce reliable estimates, and risk assessments that may not accurately assess the risk of improper payment.

**Is possible, please provide a breakdown of what percentage of improper payments are due to different types of errors. For instance, how many are overpayments, underpayments, payments to the wrong payees, etc.**

OMB reported on [paymentaccuracy.gov](http://paymentaccuracy.gov) that overpayments accounted for about \$126 billion (92 percent) and underpayments about \$11 billion (8 percent) for fiscal year 2015. Additionally, agencies reported the root causes of their improper payments for fiscal year 2015 using the new, more detailed categories in OMB guidance. While GAO did not verify the accuracy of the reported root causes, the most common root causes reported in fiscal year 2015 were:

Category of Improper Payment	Percentage of Improper Payments in Fiscal Year 2015
Insufficient documentation	33.2%
Inability to authenticate eligibility	22.8%
Administrative or process error made by <u>state or local agency</u>	14.5%
Administrative or process error made by <u>other party</u> (examples include participating lenders, health care providers, and any other organization administering federal dollars)	12.4%
Other categories	17.1%

**What does GAO see as the most important focus going forward, to reduce improper payments?**

Because Medicare, Medicaid, and the Earned Income Tax Credit accounted for more than 76 percent of the fiscal year 2015 government-wide improper payment estimate, it is critical that corrective actions are taken to reduce improper payments in these programs. We have identified various strategies and recommendations that could help to reduce improper payments in these key programs.

- **Medicare:** CMS could help reduce Medicare improper payments by (1) improving the use of automated edits by requiring contractors to share information about their most effective edits, (2) monitoring postpayment claims reviews to help reduce duplication, and (3) implementing actions authorized by the Patient Protection and Affordable Care Act, such as requiring a surety bond for certain types of at-risk providers and suppliers.
- **Medicaid:** CMS could help reduce Medicaid improper payments by (1) improving efforts to ensure that Medicaid is the payer of last resort, (2) requiring states to conduct audits of payments to and by Medicaid managed care organizations (a growing portion of Medicaid expenses), and (3) strengthening program integrity by improving reporting of key data and continuing efforts to use knowledge gained from its comprehensive reviews of states to better focus audit resources.
- **Earned Income Tax Credit (EITC):** Providing IRS the authority to regulate paid tax preparers and broadening IRS's authority to correct certain errors (math error authority) could help reduce errors in EITC claims.

From a government-wide perspective, in today's fiscal environment, measuring, reducing, recovering, and ultimately preventing improper payments become an even higher priority.

Towards this end, the following key activities are necessary.

- Adopting sound risk assessment and estimation methodologies is important to better capture the magnitude of the problem.
- Identifying the root causes of improper payments is crucial in the development of specific corrective actions to reduce improper payments.
- Implementing strong preventive controls can help defend against improper payments, such as upfront validation of eligibility using electronic data matching, predictive analytic tests, training programs, and program design issues.
- Effective detection techniques to quickly identify and recover improper payments are also important to a successful reduction strategy. Detection activities include data mining and recovery audits.



**Question #6:**

GAO states in its written testimony that: *"Our simulations show that all levels of government face long-term fiscal challenges, which could affect future federal funding of intergovernmental programs, as well as the potential capacity of state and local governments to help fund and implement these programs ... our simulations suggest that the state and local government sector could continue to face a gap between revenue and spending during the next 50 years, and that state and local governments would need to make substantial policy changes to avoid these fiscal imbalances."*

**Do you have a breakdown of the fiscal imbalances facing state and local governments - for instance, the extent to which these gaps involve unfunded pension obligations relating to state and municipal employees?**

Our long-term simulations referenced in our testimony statement are based on the state and local government sector in the aggregate, rather than individual states and localities.<sup>8</sup> As is the case with the federal government, health care costs are a primary driver of fiscal challenges for the state and local sector. These costs include Medicaid and the cost of health care compensation for state and local government employees and retirees. Since most state and local governments are required to balance their operating budgets, the fiscal conditions indicated by our simulations suggest that the sector would need to make policy changes to avoid fiscal imbalances in the future.

In 2012, we reported that most state and local government pension plans have assets sufficient to cover benefit payments to retirees for a decade or more, but plans have experienced a growing gap between assets and liabilities.<sup>9</sup> Many state and local governments are taking steps to manage their pension obligations, including reducing benefits and increasing employee contributions.

<sup>8</sup>GAO, *State and Local Government's Fiscal Outlook: 2015 Update*, GAO-16-260SP (Washington, D.C.: Dec. 16, 2015). See also, GAO, *Fiscal Outlook: State and Local Fiscal Model* (2015), accessed April 1, 2016, [http://www.gao.gov/fiscal\\_outlook/state\\_local\\_fiscal\\_model/overview](http://www.gao.gov/fiscal_outlook/state_local_fiscal_model/overview).

<sup>9</sup>GAO, *State and Local Government Pension Plans: Economic Downturn Spurs Efforts to Address Costs and Sustainability*, GAO-12-322 (Washington, D.C.: Mar. 2, 2012).

**Question #7:**

According to GAO's written testimony, the *2015 Financial Report* and individual agency financial statements provide information related to risks that are not recognized in the budget, or as liabilities in the financial statements, but could affect the federal government's financial condition in the future, including the Pension Benefit Guaranty Corporation's (PBGC) financial future, existing agreements with housing government-sponsored enterprises (GSEs), and a financial crisis at the Postal Service.

With respect to the housing GSEs, GAO's testimony states that, "Although Treasury does not believe that any further draws by the GSEs are probable, the reported maximum remaining contractual commitment to the GSEs, if needed, is \$258.1 billion.

**Under what circumstances would the federal government need to commit an additional quarter-trillion dollars to the housing GSEs?**

The President's Budget for FY 2017 reports that the funding commitment cap for Fannie Mae was \$233.7 billion and \$211.8 billion for Freddie Mac under the purchase agreements. As of December 31, 2015, Treasury's cumulative investment was \$187.5 billion, which means there is roughly \$258 billion in undrawn funding capacity.

Under the agreement, Treasury will contribute capital to Fannie and Freddie when liabilities exceed assets. An additional quarter-trillion dollar commitment would be required if there was an extreme decline in the financial condition of the GSEs—a decline worse than what these entities experienced during the most recent financial crisis according to Fannie and Freddie stress tests.

The Federal Housing Finance Agency (FHFA) has adopted rules to implement Dodd-Frank and requires Fannie and Freddie to conduct annual stress tests based on scenarios provided by FHFA reflecting different sets of economic conditions. Under the severely adverse scenario (similar to the 2007-2009 crisis—deep protracted recession, high unemployment, low GDP growth, deteriorating credit, low interest rates, falling home values, and a global economic shock, among others), FHFA reported that additional draws under the purchase agreements would range between \$68.6 billion and \$157.3 billion through the end of 2016 for both

enterprises depending on the treatment of deferred tax assets (e.g., calculated with and without a valuation of tax-deferred assets).

Therefore, market conditions would likely have to be worse than the 2007-2009 crisis for them to draw the entire amount available under the agreements.

**Are there ways we could better incorporate the risks relating to PBGC, the GSEs and the Postal Service into the federal budget?**

The risks related to PBGC, the GSEs, and the Postal Service are all examples of what we call “fiscal exposures.” Fiscal exposures are the responsibilities, programs, and activities that explicitly or implicitly expose the federal government to future spending. They vary as to source of the risk, extent of the government's legal commitment, and magnitude of the potential future spending. The magnitude of future spending arising from a fiscal exposure is difficult to quantify and is not fully reflected in the budget. For example, if the government is expected to respond to major natural disasters with funding for emergency response and long-term recovery as it has in the past, but does not budget for these costs, it runs the risk of facing a large fiscal exposure at any time.

A more complete understanding of fiscal exposures can help policymakers anticipate changes in future spending and enhance control and oversight over federal resources. Improved supplemental information in budget documents could increase transparency and facilitate explicit consideration of certain exposures without introducing additional uncertainty and complexities into the budget.

We have made a recommendation to OMB and suggested action to Congress on how to consider the risk of fiscal exposures in the federal budget process. In 2003, we recommended that OMB:

- report annually on fiscal exposures, including a concise list and description of such exposures, cost estimates, where possible, and an assessment of methodologies and data used to produce cost estimates for such exposures,
- where possible, report the estimated costs associated with certain exposures as a new budget concept—“exposure level”—as a notational item in the Program and Financing schedule of the President’s Budget, and

- ensure that agencies focus on improving cost estimates for fiscal exposures.<sup>10</sup>

These steps should complement and support continued and improved reporting of long-range projections and analysis of the budget as a whole to assess fiscal sustainability and flexibility. To date, while OMB has not implemented this recommendation, the President's Budgets for fiscal years 2016 and 2017 included a chapter on federal "budget exposure" related to climate risk, such as domestic disaster response and relief, wildland fire management, and crop insurance, and the budgetary risks of these exposures. This is an important first step in recognizing this potential future spending, but we continue to believe implementation of our recommendation would help improve budget decision making.

To better recognize the full cost of government programs and activities, in 2007, we examined other nations' experiences with accrual budgeting.<sup>11</sup> Our study of these countries and our own work confirmed the need for better information to make trade-offs between individual programs and to increase attention on longer-term fiscal challenges. In this report, we suggested that Congress may wish to expand the use of accrual budgeting to other budget program areas where it would enhance upfront control, such as insurance and environmental liabilities. Such programs include veterans compensation, federal employee pensions and retiree health, insurance, and environmental liabilities. We continue to believe that this is an issue that is important for Congress to take action on.

In 2013, building on previous work on this topic, we again examined how best to recognize fiscal exposures in the budget, and concluded that several factors need to be taken into account in selecting an approach: (1) the extent of the government's legal commitment; (2) the length of time until the resulting payment is made; and (3) the extent to which the magnitude of the exposure can be reasonably estimated.<sup>12</sup> Expanding the availability and use of information in budget documents, including measures that can signal significant changes in the magnitude of fiscal exposures, would facilitate oversight over federal resources and could aid in monitoring

<sup>10</sup>GAO, *Fiscal Exposures: Improving the Budgetary Focus on Long-Term Costs and Uncertainties*, GAO-03-213 (Washington, D.C.: Jan. 24, 2003).

<sup>11</sup>GAO, *Budget Issues: Accrual Budgeting Useful in Certain Areas but Does Not Provide Sufficient Information for Reporting on Our Nation's Longer-Term Fiscal Challenge*, GAO-08-206 (Washington, D.C.: Dec. 20, 2007).

<sup>12</sup>GAO, *Fiscal Exposures: Improving Cost Recognition in the Federal Budget*, GAO-14-28 (Washington, D.C.: Oct. 29, 2013). See also, GAO, *Fiscal Outlook: Federal Fiscal Outlook* (2016), accessed April 1, 2016, [http://www.gao.gov/fiscal\\_outlook/federal\\_fiscal\\_outlook/overview](http://www.gao.gov/fiscal_outlook/federal_fiscal_outlook/overview).

the financial condition of programs over the longer term while providing enhanced control over future spending.

**Questions for the Record**  
**Senator Charles E. Grassley**  
**Mr. Gene Dodaro, Comptroller General, GAO**  
**Budgeting Blind: The Unreliability of Federal Financial Data**  
**Wednesday, April 06, 2016**  
**Senate Budget Committee**

**Question #1**

The GAO Financial Report found three major challenges to federal financial management. The first is the serious financial management problems at the Department of Defense. I've been working for 25 years to fix the Defense Department's broken bookkeeping system.

The DOD is required to be audit-ready by September 30, 2017. Clean, accurate audits are necessary to hold the Pentagon bureaucracy accountable to the taxpayer.

In August of last year, the DoD IG had to withdraw a much-heralded clean opinion on the Marine Corps audit because of inaccurate and unreliable accounting information and a lack of supporting documentation. And, the Marine Corps was supposed to be audit ready and small and easy compared to what lies ahead. The big ones - the Army, Navy, and Air Force - are not even close to being ready.

The Department of Defense has spent billions of dollars trying to create a modern, fully integrated finance and accounting system that is capable of producing a credible financial statement. Yet the department still has not reached that goal. The department still has not gained control of the money at the transaction level. As the Marine Corps audit taught us, transaction data is unreliable, incomplete and unsupported.

**What is the root cause of the problem?**

The root cause consists of many long-standing, uncorrected weaknesses in DOD's financial management processes, systems and controls. These weaknesses include numerous disparate systems that still have problems communicating with each other, the inability of DOD components to maintain or locate documentation to support transactions and the need for qualified and experienced financial management personnel—not only at working levels but also

in senior level positions. While the military components have been implementing new general ledger systems in recent years, these systems continue to have limitations such as handling certain types of transactions and receiving complete information from subsidiary or feeder systems. Since these systems do not always properly communicate with each other, manual adjustments are often required but not always supported. Moreover, each military component has its own set of systems which ultimately must roll up to DOD's department-wide general ledger system. These deficiencies, as well as inadequate business processes, hampered DOD from collecting and reporting financial information that is accurate, reliable, and timely.

DOD needs to address the department's and components' financial management weaknesses that were identified many years ago and which led us to designate DOD financial management as a high-risk area in 1995. Most of these weaknesses have persisted and many of them continued to be evident during the fiscal year 2015 Military Services' Statement of Budgetary Activity audit. If not corrected, these weaknesses will continue to be the major impediment to DOD's ability to pass an independent audit. Since 2010, DOD's FIAR Guidance has provided a systematic methodology for DOD components to follow to identify and resolve their financial management weaknesses so that they can achieve audit readiness. However, we have found that DOD and its components have emphasized the assertion of audit readiness by milestone dates over the implementation of effective underlying processes, systems, and controls as outlined in the FIAR Guidance.

**What needs to be done to get the DOD audit readiness initiative back on track?**

In our view, DOD will need to effectively monitor its components' implementation of the FIAR Guidance and gain assurance that the components have implemented the FIAR Guidance effectively prior to asserting audit readiness. In its approach to FIAR Plan implementation, DOD has emphasized asserting audit readiness by set dates over assuring that processes, systems, and controls are effective, reliable, and sustainable. While time frames are important for measuring progress, DOD should not lose sight of the ultimate goal of implementing lasting financial management reform to ensure that it can routinely generate reliable financial management and other information critical to decision making and effective operations.

**When do you expect DOD to be audit ready?**

To become audit ready, DOD needs to ensure that they have identified all systems and control weaknesses that prevent the agency from receiving a clean opinion, develop appropriate

corrective actions, including interim milestones, and successfully remediate such weaknesses. Through such actions DOD will have a supportable basis for determining audit readiness. Until these actions are completed, it is not possible to estimate when DOD will be able to pass an independent audit.

**If the 2017 deadline mandated by Congress cannot be met, what does Congress need to do?**

Congress should consider requiring DOD to develop and provide a detailed agency-wide corrective action plan (CAP) for resolving all open audit findings, which includes interim milestones. The detailed CAP report could be provided on a monthly or quarterly basis with enough details to describe the status of the corrective action plans and progress made. This plan should prioritize the findings and recommendations that would prevent the department from receiving an opinion on its financial statements.

This detailed CAP report should be kept current with additional findings and related CAPs as they are identified in the future. Congress should consider holding periodic oversight hearings on DOD's financial improvement efforts to review progress.

**Question #2**

According to your report, improper payments are estimated to total \$136 billion. Sixty-five percent, or nearly \$90 billion of these improper payments are in Medicare and Medicaid.

This is not a new problem. GAO designated Medicare as a high-risk for fraud in 1990 and Medicare in 2003, due to the susceptibility to mismanagement and improper payments and concerns about the adequacy of fiscal oversight.

We need to be sure that CMS is doing all that it can to reduce and eliminate waste and fraud. I presume the GAO has provided ongoing recommendations to CMS to reduce improper payments in Medicare and Medicaid.



**What are the status of those recommendations?**

Since the beginning of fiscal year 2011 (the past 5 full fiscal years), GAO has made 51 recommendations to CMS related to improper payments in Medicare and Medicaid and 31 of these recommendations remain open as of April 14, 2016.

**Are there any GAO recommendations that CMS have failed to implement?**

CMS has agreed with almost all of the outstanding 31 recommendations, but is still in the process of implementing them. Given the size and growth of improper payments in the Medicare and Medicaid programs, we would encourage CMS to expeditiously implement these remaining 31 recommendations, which we believe could help curtail improper payments. Among these recommendations, we believe that those highlighted below merit the highest priority for implementation.

Medicare

- **Improving use of automated edits.** In November 2012, we reported that use of prepayment edits saved Medicare at least \$1.76 billion in fiscal year 2010, but savings could have been greater if prepayment edits had been more widely used. To promote greater use of effective prepayment edits and better ensure that payments are made properly, we recommended that CMS require Medicare administrative contractors to communicate information about their most effective edits with each other and improve automated edits that assess all quantities provided to the same beneficiary by the same provider on the same day, so providers cannot avoid claim denials by billing for services on multiple claim lines or multiple claims.
- **Monitoring postpayment claims reviews.** In July 2013, we found that although postpayment claims reviews involved the same general process regardless of which type of contractor conducted them, CMS had different requirements for many aspects of the process across the four contractor types. Some of these differences might impede efficiency and effectiveness of claims reviews by increasing administrative burden for providers. Furthermore, in July 2014, we reported that while CMS had taken steps to prevent its contractors from conducting certain duplicative postpayment claims reviews, CMS did not have reliable data or provide sufficient oversight and guidance to measure and fully prevent duplication. To improve the efficiency and effectiveness of Medicare program integrity efforts, we recommended that CMS reduce differences between contractor postpayment

review requirements, when possible, and monitor the database used to track recovery audit activities to ensure that all data were submitted, accurate, and complete.

- **Implementing actions authorized by the Patient Protection and Affordable Care Act (PPACA).** We reported in our February 2015 update to our High Risk series that CMS should fully exercise its PPACA authority related to strengthening its provider and supplier enrollment provisions, such as requiring a surety bond for certain types of at-risk providers and suppliers.

#### Medicaid

- **Improving third-party liability efforts.** There are known challenges to ensuring that Medicaid is the payer of last resort. For example, states have reported challenges working with private insurers, including a lack of willingness to release coverage information to states and denial of claims for procedural reasons. While CMS has issued a guide on effective state practices, we recommended an additional action that could help to improve cost-saving efforts in this area, in particular, providing guidance to states on oversight of third-party liability efforts related to Medicaid managed care plans.
- **Increasing oversight of managed care.** In May 2014, we reported that most state and federal program integrity officials we interviewed told us they did not closely examine managed care payments, focusing on fee-for-service claims instead. To help improve the efficiency and effectiveness of program integrity efforts, we recommended that CMS require states to conduct audits of payments to and by managed care organizations, update managed care guidance on program integrity practices, and provide states with additional support in overseeing managed care program integrity.
- **Strengthening program integrity.** CMS has taken positive steps to oversee program integrity efforts in Medicaid, including implementing certain recommendations we made. CMS needs to take action to address issues and recommendations that have not been fully implemented, such as ensuring that data on ineligible providers are more readily accessible, strengthening its efforts to calculate return on investment for its program integrity efforts, and continuing to use knowledge gained from its comprehensive reviews of states to better focus audit resources and improve recovery of improper payments.

#### **And finally, are there any actions that Congress can take in this area?**

Our recommendations related to Medicare or Medicaid improper payments to providers have been directed to the Administration. Additional Congressional oversight of HHS actions will help maintain emphasis on reducing improper payments in these important programs.

## **BUDGETING FOR OUTCOMES TO MAXIMIZE TAXPAYER VALUE**

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**WEDNESDAY, APRIL 13, 2016**

U.S. SENATE,  
COMMITTEE ON THE BUDGET,  
*Washington, D.C.*

The Committee met, pursuant to notice, at 10:31 a.m., in Room SD-608, Dirksen Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Crapo, Ayotte, Perdue, Whitehouse, Stabenow, and Kaine.

Staff Present: Eric Ueland, Republican Staff Director; George Everly, Chief Counsel; for the Minority: Joshua Smith, Budget Policy Director.

### **OPENING STATEMENT OF CHAIRMAN ENZI**

Chairman ENZI. Good morning. I will call to order this hearing. It is the second hearing in a series this Committee is holding on America's broken budget process.

Everyone here already knows what the problems are. Our congressional budgets are no longer governing documents and are increasingly ignored, leaving the country without a long-term plan. When we actually do our appropriations bills, they are months late, increasing uncertainty for agencies and businesses, and 70 percent of the budget is operating on autopay and will eventually bankrupt the country if Congress does nothing.

It is long past time for a serious, constructive conversation about how we fix our broken budget process. I am looking forward to working together to explore new and innovative approaches to how we allocate our Government's limited resources.

Last week, we heard from the Comptroller General that the Federal Government cannot even tell us all the assets we own. Congress rarely, if ever, actually looks at what happened to the money we have already spent. Instead, we are constantly focused on how to spend this year's new money.

When Congress spends money on a program, it should also spend time understanding how effective that program has been in the past and what resources are devoted to that goal with an eye to successful outcomes and the highest value for taxpayer dollars.

Today we will discuss different approaches to budgeting and oversight that inject this much needed information into Congress' resource allocation decisions. Unfortunately, our current budget process encourages incremental, isolated decisionmaking that focuses on spending rather than results.

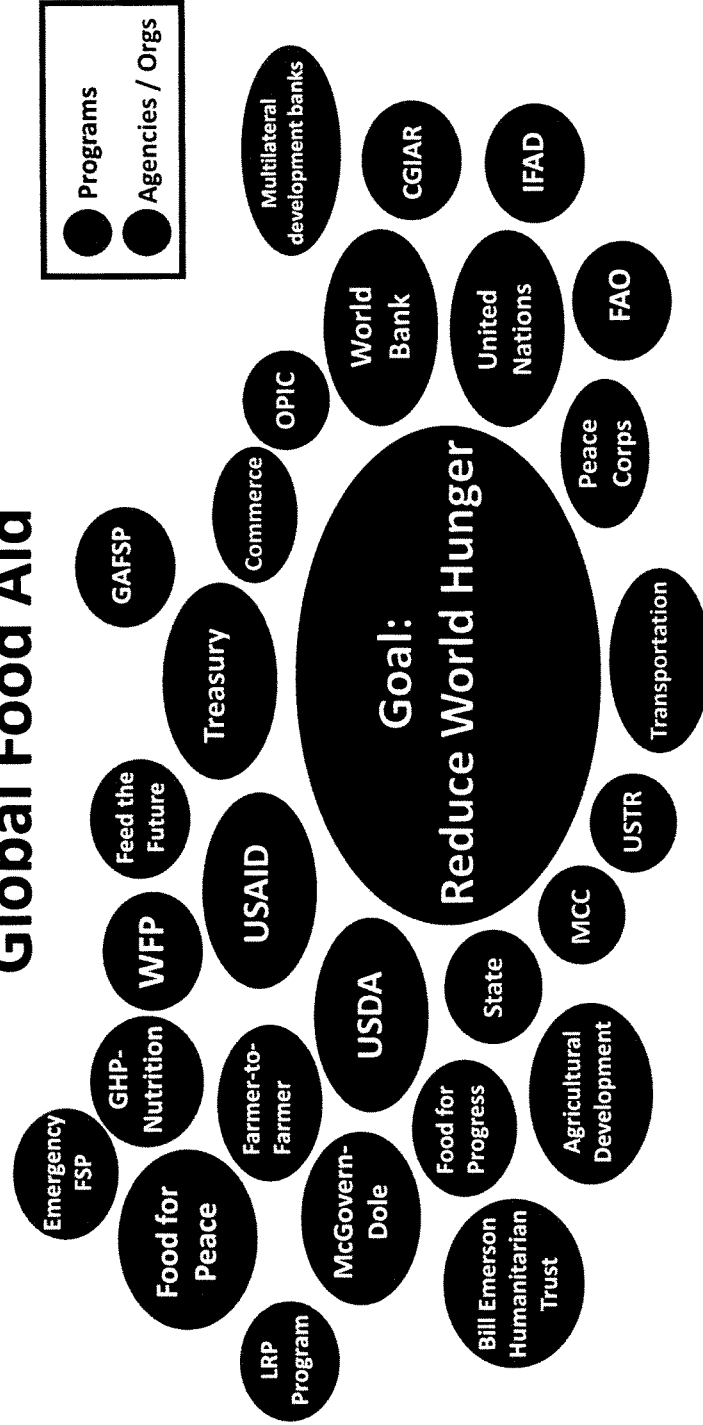
Our main budget tool is a baseline that locks in current policies. This forces an incremental approach to budgeting that results in only marginal changes to funding levels. Congress frequently ends up debating how much more or less funding a particular program should receive compared to the baseline rather than whether the funding that program has already received leads to the desired outcome.

The budget process also lacks a mechanism to prioritize funding for policy goals across different Government programs. The Government Accountability Office, GAO, has been warning us for years about the growing number of duplicative, overlapping, and fragmented Government programs. Many of the problems highlighted by the GAO stem from the fact that our budget decisions are made within silos within Federal agencies and congressional committees whose jurisdictions overlap. This has led to an unmanageable mess of competing programs and bureaucratic inefficiencies.

Take international food aid, for example. The Federal Government spends billions of dollars each year on programs intended to reduce world hunger by providing food commodities and educating local and regional farmers in low income countries. Instead of reforming existing programs, the Government creates new ones, more of them, increasing inefficiencies, increasing duplication and fragmentation within and across agencies.

If you look at the chart on the screen, you will see how the Federal Government has approached its goal of reducing world hunger. The blue circles show 12 different Federal agencies that work toward this goal. The green circles represent the 16 different Federal programs with its own source of funding, all meant to reduce global hunger. That is 12 agencies controlling 16 different programs, all trying to accomplish the same goal.

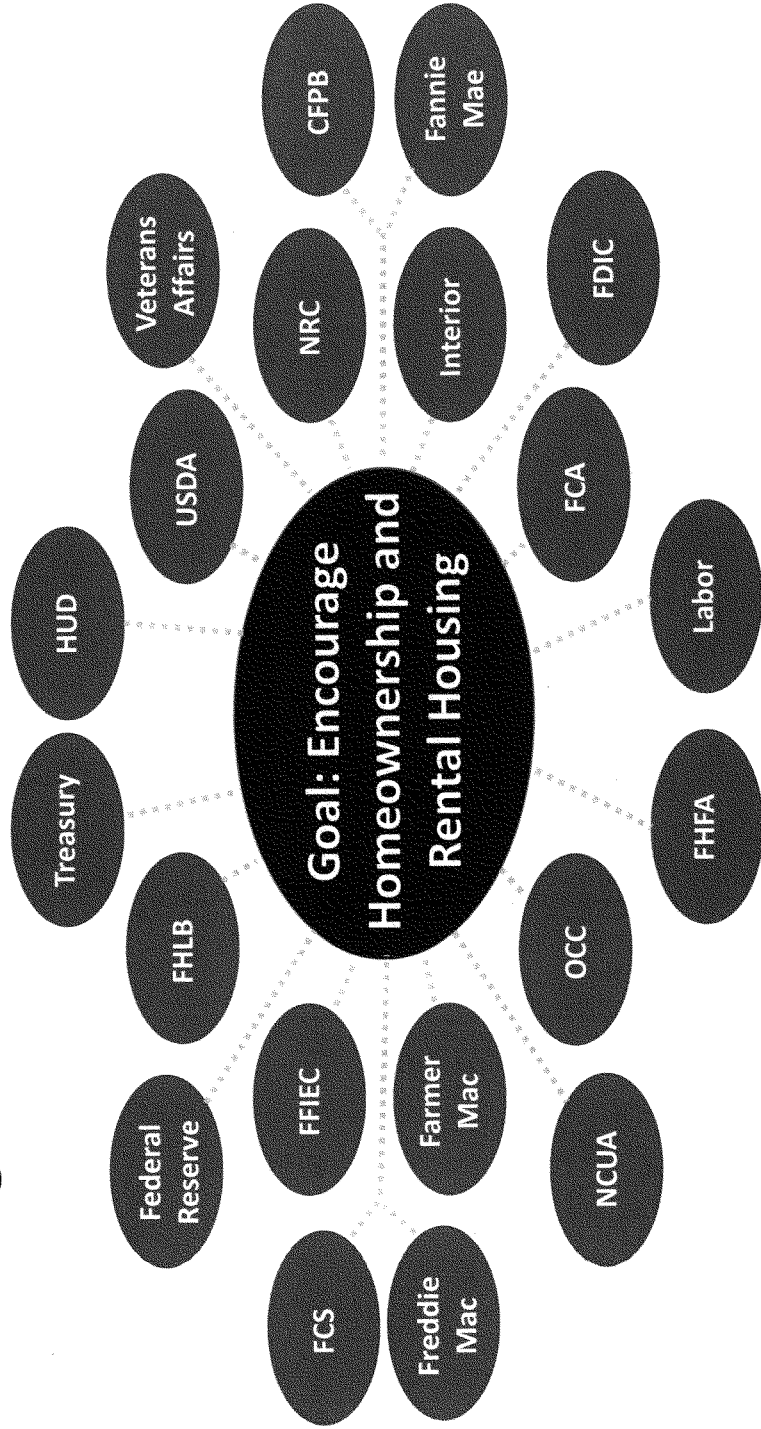
# 12 Agencies and 16 Programs Contributing to Global Food Aid



Oxfam America estimates that 59 cents of every dollar meant for food goes to outdated regulations and program inefficiencies, wasting up to \$471 million each year. A better budget process would have streamlined these programs by focusing on the overall goal, thereby cutting waste and achieving better outcomes.

Another example of duplication and overlap is Federal housing assistance. The chart on the screen shows you 20 Federal entities that oversee 160 different housing programs and tax preferences devoted to promoting homeownership and affordable rental housing. The blue circles represent all the different agencies that are devoting resources to this goal. The programs are not included because there are so many of them, we could not fit them on the screen. These initiatives cost the Government \$170 billion in 2010. GAO found that many of these 160 programs overlap and that money could be saved by consolidating and streamlining them. Agencies could be doing more with less, helping more people to purchase their first home or to find their family a better place to live. But by acting inefficiently and spreading its resources across so many programs, each of which, of course, needs managers and assistants and secretaries and so on, the Government is not maximizing the good it intends to do. By changing the way we think about budgeting, we can make Government more effective and efficient and better able to serve our constituents.

## 20 Agencies Oversee 160 Housing Programs



Finally, the budget process does not set goals or ask whether Federal funding accomplished what it was supposed to. We budget by looking at the inputs for each individual program rather than all the resources devoted to achieving a particular goal. So, essentially, Congress does not even have a good way of knowing whether the money it previously spent was effective at achieving the policy goal.

This problem has been exacerbated by the growing share of mandatory funding in the budget. Mandatory programs operate on autopay without the need for congressional review. So there is absolutely no connection between funding decisions and program performance. Given that this spending often continues in perpetuity, there should be a formal mechanism to ensure that taxpayer money is being spent wisely. There really ought to be some kind of criteria, too, for why we make a program mandatory. One of those criteria might be that it has its own source of revenue, such as Social Security.

Our budget process should help us allocate taxpayer resources to produce desired policy goals effectively and efficiently. To make these decisions, Congress and the agencies need to know at least two things:

First, we must have a detailed accounting of all of the resources that are being devoted to a particular policy goal and how those resources interact with each other. In other words, a decision to fund a certain program should be informed by all the other programs and resources already devoted to that goal.

Second, decisionmakers need to know whether programs are performing effectively and whether they are achieving the desired outcomes. The program with the best performance should receive more funding, and poorly performing programs should receive less or maybe none at all. The Government Performance and Results Act, as recently amended, provides a good starting point for this analysis, but the information provided under that act needs to be connected to congressional and executive decisionmaking.

This Committee has an opportunity to fundamentally reexamine the way Congress and executive agencies allocate resources. It is time for a better budget process, one that maximizes values received from taxpayer dollars. And I look forward to working with my colleagues. I think that this is the only time in the next 4 years we are going to be able to make the kind of changes that we need to make, and that is because at this point in time no one knows who the next President is going to be and no one knows who the majorities are going to be in Congress. So both sides should be willing to act and to act reasonably, and I look forward to working with that, and I look forward to working with my colleagues to explore these new ideas on how to make our budget work more effectively and efficiently.

Senator Whitehouse.

#### **OPENING STATEMENT OF SENATOR WHITEHOUSE**

Senator WHITEHOUSE. Thank you, Chairman Enzi, and I appreciate your comments. I would say that there may be valid reasons why some programs are separated out. You used the example of housing programs. In Rhode Island, we have a problem of veterans'



homelessness that I think we share around the country. When you are dealing with veterans, I think you are probably actually better off working with veterans' organizations and working with veterans' funding and working with the Veterans Administration. So the fact that there is a special program for housing for veterans to me is not a sign of weakness, necessarily, and I think as we look at this, we need to bear those common-sense distinctions in mind.

I appreciate very much your attention, Mr. Chairman, to budget process reforms, including proposals such as portfolio budgeting, which is the focus of today's hearing. With major policy areas such as higher education and oceans and coastal resiliency spanning the jurisdictions of multiple Senate committees, the Budget Committee may be able to play a valuable role in offering big-picture recommendations to improve outcomes and make Federal investments more efficient. I look forward to hearing on that subject from our witness panel.

I know also that the Chairman has been working hard on his own proposal to move to a biennial budget process, a reform that has long garnered bipartisan interest. While many Democrats, including myself, would be open to a budget resolution that spans 2 years, I believe there is far less support for shifting to a 2-year appropriations cycle, particularly among appropriators.

I also want to note that Democrats on this panel would likely oppose any proposals that would put defense appropriations on a different schedule from the bills that fund education, housing, health care, veterans' benefits, and other vital domestic programs.

I hope this Committee will be able to craft bipartisan biennial budgeting legislation that considers these concerns. Given that it does not seem our Committee will produce a budget resolution this year, we could use this time to evaluate budget reforms that could make the process smoother in future years.

In addition to biennial budgeting, there are a number of other proposals I outlined earlier this week in a letter to the Chairman, which I would ask unanimous consent to put into the record.

Chairman ENZI. Without objection.

[The letter follows:]

SHELDON WHITEHOUSE  
RHODE ISLAND

COMMITTEES  
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## United States Senate

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April 11, 2016

Hon. Mike Enzi, Chairman  
United States Senate Committee on the Budget  
Washington, DC 20590

Dear Chairman Enzi:

Thank you once again for your leadership in exploring ideas to improve the congressional budget process and revive the relevance of the Senate Budget Committee. As you continue to work on your biennial budgeting proposal, I write to encourage you to consider other potential process reforms, including the ones I outline below. Given that the Committee will likely not produce a budget resolution this year, I hope we will have the opportunity to consider bipartisan legislation to lay the foundation for a smoother budget process in future years.

### Reconciliation Reform

In 2009 testimony before the Budget Committee, the late Senator Robert Byrd said, “The reconciliation process was designed to facilitate legislation to reduce deficits. Instead, the process has been used to enact multi-trillion-dollar tax cuts that led to record deficits over the last eight years.” Under the prior majority, Chairman Kent Conrad added a temporary rule that reconciliation bills must reduce the deficit, but this rule is no longer in effect. Reconciliation reform could ensure the fast-track process is only used to facilitate the passage of deficit-cutting legislation.

### Prohibit Budget Points of Order against Incidental Violations

Non-budgetary legislation—for example, a measure to establish a new criminal penalty—can trigger budget points of order by having as little as a \$500,000 effect on the federal budget. These incidental points of order do little to help us enforce the congressional budget, and diminish the value of points of order when the Senate is considering budgetary legislation. We should consider amending the Budget Act to prohibit points of order against incidental violations.

### Require More Transparency about How Proposed Budget Cuts Affect Programs

The FY 2016 budget resolution proposed trillions of dollars in spending cuts without specifying programs, accounts, or even committees of jurisdiction. We could improve honesty in budgeting by requiring the budget to assign any proposed spending cuts to a committee or committees of jurisdiction.

### Debt Ceiling

Debt-ceiling brinksmanship hurts our economy and undermines faith the world has in our financial markets. Majority Leader McConnell crafted a thoughtful solution to this problem, the so-called McConnell Rule, a temporary version of which allowed President


Obama to raise the debt ceiling several times, subject to a congressional disapproval process. We should consider making the McConnell rule permanent, perhaps tied to the debt levels adopted in the budget resolution.

**Vote-a-rama Reform**

Budget vote-a-rama reflects poorly on the Senate as an institution. Any number of reforms could bring some sanity to the process while protecting the rights of the minority. For instance, each side might be permitted roll call votes on ten amendments with an additional five side-by-sides. With a fixed number of votes, floor managers might be able to spread them throughout the week, ending Senate consideration of the budget resolution at a reasonable time.

Once again, I hope you will consider exploring process reforms, including these, in the Budget Committee this year. I believe that if we work together, we can agree on bipartisan reforms that will improve the budget process next Congress, no matter which side holds the majority.

Sincerely,



Sheldon Whitehouse  
United States Senator

cc: Senate Budget Committee Members

Senator WHITEHOUSE. This has largely transpired because the Senate has moved from being an ordinary majority vote body to being an ordinary super majority vote body in which, as Majority Leader McConnell has said, if it is important, it needs 60 votes. Well, the budget is important, and the appropriations bills are important, and they tend to need 60 votes, which makes the 60-vote penalty threshold for violating the budget a complete moot penalty. And it disables the effect of this Committee, and that is one reason that we always meet here with lots of empty chairs, and everybody knows the Committee really does not matter much any longer.

So here are some suggestions to help us run a little better.

First, we could tighten up the reconciliation process to ensure that this procedural shortcut can only be used to actually reduce the deficit. In 2009 testimony before this Budget Committee, the late Senator Robert Byrd said, "The reconciliation process was designed to facilitate legislation to reduce deficits. Instead, the process has been used to enact multi-trillion-dollar tax cuts that led to record deficits over the last 8 years." With a short and simple clarification, we can ensure that reconciliation will focus on the deficit.

We could also review Budget Act points of order to ensure that they are working as intended to enforce the budget framework. I have seen potential Budget Act points of order hold up non-budgetary legislation over de minimis violations. Budget enforcement tools are important, but they should be used to maintain discipline on deficit spending, not to hamper legislation generally.

We could also improve the transparency of the Committee's budget resolution by requiring proposed spending cuts or increases in our budget to be assigned to specific committees of jurisdiction, or perhaps in some cases even to actual programs. If a budget proposes deep spending cuts, the American people could better understand what that would actually mean.

Another area that I believe is ripe for bipartisan legislation is the debt ceiling. According to GAO, last minute debt ceiling brinkmanship can be costly. The agency estimates that just the threat of default increased borrowing costs during the 2013 impasse by tens of millions of dollars. Leader McConnell crafted a thoughtful solution to this problem, a temporary version of which allowed President Obama to avoid a debt default, subject to a congressional vote of disapproval. We could work on a bill to make the McConnell rule permanent, perhaps tying it to the deficit numbers in the budget resolution.

Finally, if we are interested in a smoother budget process, we could address the foolishness of the annual budget vote-a-rama and its pandemonium of late-night voting. Any number of reforms could help bring some sanity to the process while still protecting the rights of the minority party.

For instance, each side might be permitted roll call votes on a fixed number of amendments, say ten amendments each, with an additional five side-by-sides. With a fixed number of votes, floor managers might be able to spread them throughout the week, assuring Senate consideration of the budget resolution at a reasonable time and in a reasonable manner. The budget process need not every year devolve into partisan pandemonium.

These are, of course, just a few reforms we might consider pursuing in what is shaping up to be an unofficial off-year without a budget resolution.

I once again commend Chairman Enzi for his attention to process reforms, and I look forward to working with him on bipartisan legislation.

Chairman ENZI. Thank you, Senator Whitehouse.

I think we all agree there are some serious problems the way Congress exercises its tax and spending powers, and fixing America's broken budget system needs to require some innovative approaches and tough decisions, and you just named a number of them. So I am confident that there are some solutions out there that we can work together on.

Senator WHITEHOUSE. And I am confident that there are others as well that other members of the Committee would be happy to share.

Chairman ENZI. And that is what I am hoping will happen, partly as a result of the hearings, and that is why the hearings we are having this month will be designed to find out more about what is being done and what could be done. And I think we have some great people here today that will help us with that.

We have Dr. Paul Posner, who is the Director of the Graduate Public Administration Program for George Mason University and leads the university's Center on Public Service. He is the past president of the American Society for Public Administration and is a board member for the National Academy of Public Administration. He is also currently co-chair of the National Budget Roundtable.

Ambassador Maurice McTigue is a vice president of the Mercatus Center at George Mason University. He is a former cabinet minister and Member of Parliament in New Zealand. That is one of my favorite countries because it is usually abbreviated as "NZ". [Laughter.]

I have some ties that have that on them.

He pioneered innovative approaches to budgeting that helped reform his country's public sector. He also served as advisor to the Office of Management and Budget during the Clinton and Bush administrations on issues of accountability and transparency and has consulted with legislators and Governors in more than 30 States.

Our third witness is Dr. Roy T. Meyers. He is a professor of political science and public policy at the University of Maryland, Baltimore County. He worked previously for the Congressional Budget Office and is currently a fellow at the National Academy of Public Administration.

I thank all of you for joining us today. One of the things that we also traditionally do, partly because members have a number of obligations and sometimes are not here, I appreciate the testimony that you presented that we can all look over. Sometimes more can be absorbed by reading than by listening. We are not known for our listening. And at the conclusion of this, I will be announcing that they can turn in written questions, which we would appreciate you answering as promptly as possible as well.

So, Professor Posner.

**STATEMENT OF PAUL L. POSNER, PH.D., DIRECTOR OF GRADUATE PUBLIC ADMINISTRATION PROGRAM, SCHOOL OF POLICY, GOVERNMENT, AND INTERNATIONAL AFFAIRS, GEORGE MASON UNIVERSITY**

Mr. POSNER. Thank you, Mr. Chairman, Senator Whitehouse, Senator Perdue. I am pleased to be here to share my views on the way to move to a more strategic way to allocate resources within the congressional budget process. You have testified far more eloquently than I can about the broken budget process. What I want to do is focus today on what I think is the role the budget process can play in changing our focus in budgeting away from the line items and the like to a broader view of what is the purpose for which we are allocating resources. How could we make those allocations in a way that is more mindful of the outcomes we are trying to achieve?

Today, for the most part, in the budget process we have a variety of programs that are located in different committees, in different sectors of the budget. Tax expenditures, spending, regulations, and like—all of them are walled off from one another. There is no comprehensive way to compare claims in areas like food safety, job training, and the like where there are so many programs that compete for funding.

In my statement today, I provide a vision for beginning to deliver on what was the original promise in the 1974 act, which was to try to provide a more comprehensive prioritization of limited resources for the Nation. I do this knowing that it is going to be very difficult for any reform in this Congress, or any Congress, really, to go through. But I do this knowing that at some point we are going to have to make hard choices again. Perhaps not today but at some point in the future, knowing the long-term projections of CBO, GAO, and others, we are going to make hard choices, and it is better to have approaches to rationalize those choices on the shelf that have been discussed in forums like this rather than to do so in the heat of a crisis.

And basically what I am suggesting is Congress dip its toe in the waters of prioritization through what I and my co-author of the concept here, Steve Redburn, call “portfolio budgeting.” This is not zero-based budgeting where we put everything on the table and try to make sense of it all at once. It is not even performance budgeting where everything gets measured. It is more selective and focused, and it kind of embodies the spirit of what David Stockman used to say: Budgeting should be about ferreting out weak claims, not weak claimants. Compare comparable programs in different areas and make the wisest choices based on which programs are the most cost-effective way to use resources.

Essentially what we are doing is what other nations in the OECD call “program review.” Almost every nation does it. Australia, New Zealand, Netherlands, Canada do a selective review of portions of the budget focused on common goals. In my testimony, I talk about higher education and housing as two case studies where each area is rife with subsidies from the tax and spending side across different committees and programs that have really never been pulled together and rationalized to address common

issues. And that is the kind of thing that I think the promise of portfolio budgeting gives us.

It is very difficult to look at any program and find that a single program encompasses the sum of Federal activities. For almost everything the Federal Government does, there are many different programs that are fragmented across the board. And so portfolio budgeting gives the opportunity to take a look at those systematically, weed out the ones that are most inefficient, identify programs that are contradictory or redundant, and reprioritize.

One example of that would be the flood insurance programs and disaster relief where, on the one hand, we are trying to get people to ensure properties for flood; on the other hand, we are being so generous, we are letting people occupy hazardous lands that eventually set us up for extraordinary costs in disaster relief. So it is a way to kind of take stock of our programs.

In some ways, the portfolio budgeting process is a way for Congress to seize the high ground from the executive, which frequently looks at policy reviews. The program rating tool that the Bush administration used, for example, looked at every program in the budget, and they applied a common tool to assessing how well those programs were doing. That was a very exhaustive way to do this process, but it did not really group programs together against common objectives, and that is, I think, what we are talking about here.

It may seem that what we are asking Congress to do here might be high-minded but very difficult to do, and certainly it is. But I have seen this Committee use task forces before. In 2000, Senator Domenici was Chair. There were four task forces that were formed to look in-depth, deep dives on areas like the international assistance account or elementary and secondary education.

I think we can think about that kind of process here again with the Budget Committee. To me, the Budget Committee is the perfect Committee to look across the different programs and tools at these portfolios and do some selective reviews that could then be integrated into the budget process. We might call it a "performance-related reconciliation process," where we take a savings target and we provide it to a task force that is looking at higher education assistance, for example, which we now fund at \$130 billion a year. And we expect that committee to come up with some improvements in the program and policies as well as some dollar savings that flow from those improvements.

That is the kind of process I have in mind. This Committee probably, arguably, should do this in concert with the authorizing committees. Ultimately, it may be important for this Committee to reconceptualize its role as a leadership Committee and stock itself with members, from other committees that are leadership committees such as Finance and even some of the authorizing committees, to really bring about a holistic approach to this problem.

Thank you.

[The prepared statement of Mr. Posner follows:]

**Portfolio Budgeting: A New Strategy for Budgeting**

**Statement of Dr. Paul L. Posner,  
Director of Graduate Public Administration Program  
School of Policy, Government and International Affairs  
George Mason University**

**For**

**Hearing before**

**The Committee on the Budget**

**United States Senate**

**Wednesday, April 13, 2016**



Chairman Enzi, Ranking Member Sanders and other Members of the Committee,

I want to thank you for inviting me to share my thoughts with you on Congressional budget reform. I commend the Committee for taking on the important but challenging project of federal budget reform.

In many respects, the high-minded goals of the 1974 Congressional Budget Act have been eclipsed by tenacious partisan polarization, a fragmented congressional committee structure and strong pressures from stakeholders to avoid tampering with existing priorities and programs. The federal budget process has become embroiled in polarized politics, at times barely able to keep the government open and financed. When it does achieve this very minimalist goal, it does little beyond providing an allowance for discretionary appropriations. And these ceilings have become increasingly symbolic statements rather than politically realistic targets to guide appropriations decisions. Budgeting has become less an arena to solve fiscal and policy problems together and more of a staging area where positions are taken for primary constituencies and other audiences far removed from running the government.

As a result, the current budget process does not enable Congress to achieve three important objectives: (1) set fiscal policy likely to keep the nation's economy on a sustainable course, both for today and the longer term; (2) allocate resources to assure that scarce resources are used to support the highest priorities; and (3)

ensure that government is equipped to deliver public services in the most efficient and effective way possible.

While much commentary has been devoted to the impact of the process on deficits and fiscal policy, the legitimacy of fiscal policy is critically dependent on the composition of spending and taxes that are used to reach fiscal targets. I will focus today on how the budget process affects the allocation of budgetary resources across the numerous claims that compete for scarce resources. . Simply put, the budget process has failed to fulfill the expectations of the 1974 Act to become a vehicle to prompt a comprehensive review of priorities across federal programs and funding tools. Most of the federal budget is insulated from periodic reviews, as disproportionate attention is paid to the shrinking discretionary spending sector of the budget. The caps on discretionary spending in the budget resolution largely constitute symbolic targets rather than a real set of constraints – targets that often prove to be unenforceable without resorting to a set of increasingly pervasive gimmicks and sleights of hand.

Of course, there are many reasons much of the budget is not subject to periodic review and assessment. Mandatory spending and tax expenditures are, by design, protected from annual reviews in the interest of promoting certainty for beneficiaries and economic actors. Periodically reexamining these and other commitments entails difficult political choices for the Congress and the President alike, particularly in times when there is no surplus to celebrate. The Congress is

fragmented across its committees, which can be expected to resist the imposition of constraints or targets by the budget committees or even by the leadership if constraints require making hard choices among competing claims and constituencies. Nonetheless, the Congress itself has engaged in hard choices periodically, reforming welfare, social security and achieving budget surpluses in the 1990's. Should the deficit and other forces rear their head in a compelling way, Congress may wish to turn to a process that permits itself to more comprehensively rank and prioritize existing claims on the budget.

Much of the remainder of this statement considers whether and how the Congressional budget process can become a vehicle to prompt Congress to rationalize priorities based on a more comprehensive, strategic review of priorities and performance. Ideally, a budget process should be informed by evidence comparing the relative performance of related programs. As one former budget director stated, budgeting should concentrate on ferreting out weak claims, not weak claimants. As we face up to rising deficits in the years ahead, a performance assessment process may help lay the groundwork for making choices that not only resolve underlying fiscal deficits but also promote improved performance by reexamining existing program commitments. Ideally, such a process would consider the entire portfolio of federal programs and activities addressing a single policy goal or a set of related goals and outcomes. The portfolio would include mandatory and discretionary spending as well as tax expenditures – using a process we call portfolio budgeting.

**Allocating scarce resources: the inescapable challenge for budgeting**

Ideally, a budget process should facilitate informed tradeoffs among competing objectives, programs and tools of government. Former Congressman Charles Stenholm best described the competition that the congressional budget process was intended to inspire: "This process will require many tough choices as priorities are set among worthy programs. But essentially, all programs will be together in the same boat, competing for priority status as we seek to determine how best to allocate the revenues coming into the U.S. Treasury."

I am concerned that the congressional budget process has strayed far from the vision of Mr. Stenholm and other guardians of the fiscal commons. The tradeoffs and hard choices that budgeting requires are far more difficult to achieve under our current political system than the one we had when the Congressional Budget Act was passed in 1974.

The current budget process is highly balkanized, with high walls separating programs in discretionary, mandatory and tax expenditure sectors. Related programs for such federal policies as higher education assistance or low-income housing are splintered across this fragmented budgetary landscape. While the budget resolution discusses the 19 budget functions that provide a mission oriented

framework integrating related programs across the budget, these potentially helpful categories are not, in fact, used to prompt appropriators or authorizers to consider how to allocate scarce resources across these competing functions.

Discretionary spending bears the disproportionate impact of meeting fiscal targets and constraints, while existing tax and spending entitlements continue to drift upward with no regular review and little or no limits. Discretionary spending has declined from 9.3 percent of GDP when the Budget Act was passed in 1974 to less than 7 percent today, while mandatory programs have doubled during the same period to 13.5 percent of GDP. Tax expenditures, which function much like spending programs, are estimated at 8 percent of GDP, exceeding discretionary spending, and yet escape regular review. Deficit reduction plans can achieve greater savings in a more balanced way if they are applied against a broader base including spending and tax entitlements. While cutbacks are never easy, they are likely to be perceived as more fair if levied against all claims in the budget affecting all major stakeholders. Fiscal history tells us that stakeholders are not likely to accept the legitimacy of cuts if they are singled out, raising fears that their sacrifice will be exploited by champions of other budgetary claims.

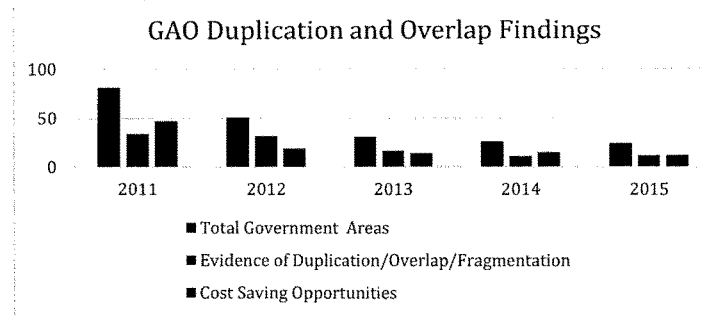
As we think about priorities for using resources, it has become more apparent that the important goals and objectives of policy cut across the narrow confines of programs, budget accounts, bureaus, and congressional committees. For instance, nearly one half of the budget authority for homeland security is provided by

numerous agencies outside the Department of Homeland Security. Indeed, most of the major missions of government transcend the boundaries of the federal government itself, requiring partnerships with state and local governments, nonprofit organizations and for-profit firms.

The inventory of duplicative and overlapping programs compiled periodically by GAO is one reflection of rampant fragmentation across the federal landscape in programs addressing common goals.<sup>1</sup> Often the product of adaptive responses to emerging problems, the common response has been the proliferation of responsibilities and programs, perhaps targeted to a new clientele, or involving a new program delivery approach, or even simply merely layered onto existing systems and programs. GAO's five reports issued from 2011 through 2015 detail over 200 program areas with either significant fragmentation, overlap or duplication as well as other cost savings opportunities.

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<sup>1</sup> Government Accountability Office, *2015 Annual Report: Additional Opportunities to Reduce Fragmentation, Overlap and Duplication and Achieve Other Financial Benefits*, GAO-15-404SP, April 2015



Profound institutional barriers to prevent easy tradeoffs between spending programs across different agencies and committees to address endemic program fragmentation. While the declining share of budgets devoted to discretionary spending are reviewed each year, periodic reviews of mandatory and tax expenditure programs are generally not encouraged. Tradeoffs between spending programs and tax expenditures are strongly discouraged, even though tax provisions and spending programs both address common purposes such as financing higher education, child care, job training, low income housing or research and development.<sup>2</sup> Split or shared ownership of these tools by different congressional committees and federal agencies constitutes the most significant barrier to their cross-cutting review in the budget process.

A focus on outcomes could support a cross cutting focus, because achieving most outcomes engages the resources of multiple programs, many agencies and

<sup>2</sup> U.S. Government Accountability Office, *Government Performance and Accountability: Tax Expenditures Represent a Substantial Federal Commitment and Need to Be Reexamined*, GAO-05-690, 2005.

nonfederal actors alike. The traditional unit of analysis in budgeting, however, is the budget account and the federal agency, with little opportunity to recognize the crosscutting dimensions of performance or to identify alternative strategies that would be a much more productive use of resources to drive achievement. For the most part, appropriated programs are reviewed in the annual process in an isolated way, typically with a focus on the marginal or incremental change in resources from one year to the next.

#### **A Portfolio Approach to Reexamining the Base**

A performance assessment process may help lay the groundwork for making budget choices that not only address macro fiscal goals but also promote more cost effective use of resources to achieve major policy goals. Such a process would consider the entire portfolio of federal programs and activities addressing a given goal, including mandatory and discretionary spending as well as tax expenditures. It would take advantage of the information on goals and performance Congress mandated be developed when it passed the 2010 Government Performance and Results Act Modernization Act, and take advantage of the Act's requirements for consultation with Congress when policy objectives are established.

The portfolio budget process I have in mind would assess the collective impacts of what are today fragmented initiatives and examine the likely benefits and costs of budget alternatives. The process would ask questions about the collective



performance of the portfolio of programs considered together. It would seek to identify:

- Which activities and programs constitute the portfolio and how much budgetary resources do they consume?
- Which current programs and policies are more cost-effective in achieving these goals?
- Which programs are considered to best achieve goals of fairness and equity in the distribution of benefits and costs?
- Which programs and policies are most critical in reinforcing the overall goals of the broad policy area and which undermine or work at cross purposes to those goals?
- Are there alternative ways of using limited resources that evidence suggests would be more productive than the current array of programs and policies in driving achievement of policy objectives?

Recognizing that such reviews are demanding both analytically and politically, they should be selectively deployed in the budget process. Far from zero based budgeting, portfolio budgeting should be used for areas where top officials have agreement that a deeper reexamination is most necessary.

Most nations in the OECD now use a comprehensive spending review process to periodically consider selective broader policy areas in the budget process. Many

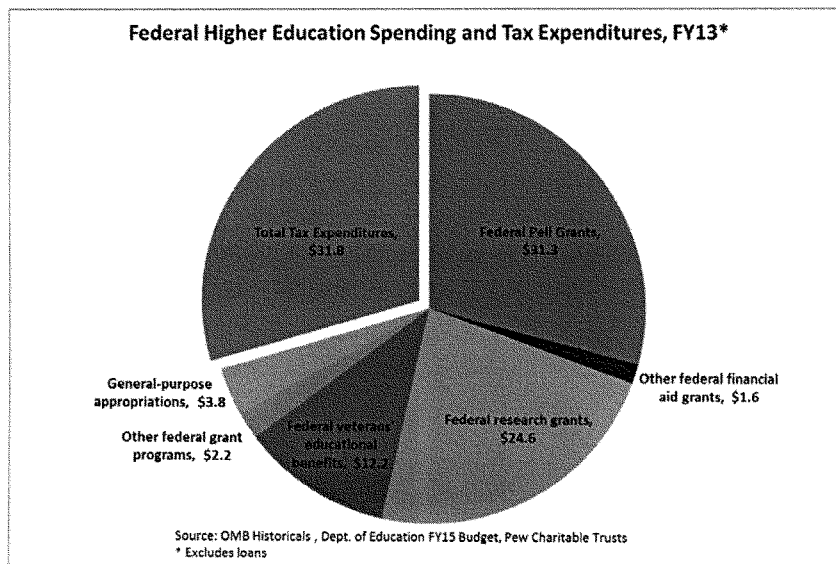
nations have learned from the Netherlands, which has been doing these reviews for at least twenty years. The 2010 spending review examined 20 topics and was designed to produce options to reduce spending by 20 percent over four years. So-called Interdepartmental Spending Reviews have been ongoing since the early 1980's, featuring a review of policy areas that cut across ministries. These initiatives have often included not only Finance and line ministry staff but also outside experts. They have led to significant savings over the years.<sup>3</sup>

For the National Budget Roundtable which I co-chair with Maya MacGuineas and Stuart Butler, my colleague, Steve Redburn, and I have developed a paper applying portfolio budgeting to policy objectives for federal aid to higher education.<sup>4</sup> The federal budget provides an array of separate grant and loan programs and tax expenditures to help students pay for college, including special programs for veterans. The chart below shows the composition of federal activity - federal spending for higher education will exceed \$75 billion, slightly more than the States are expected to spend for their public higher education institutions, with an additional \$30 billion of tax expenditures provided through eleven discrete programs in the tax code. These figures do not include federal loans, which now have a total annual volume of \$700 billion, even though such programs turn a profit for the federal budget.

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<sup>3</sup> OECD, *Reallocation: The Role of Budget Institutions*, 2003.

<sup>4</sup> Steve Redburn and Paul Posner, *Portfolio Budgeting: How a New Approach to Resource Allocation Could Yield Better Decisions*, National Budget Roundtable, Washington: Brookings, September, 2015.



While federal aid has grown, the myriad of subsidies has not been considered holistically, but rather has grown up in an ad hoc fashion, incubated in different congressional committees and federal agencies. It is ripe for review. In many ways, U.S. higher education is the envy of the world. At the same time, many questions have been raised about how effectively the current system of federal grants and loans is contributing to access by those who otherwise would not attend college and whether the increasing reliance on debt is reducing the personal economic returns that otherwise would accrue to those receiving federal support. Questions have been raised about whether federal subsidies are incentivizing states to reduce their own aid for students and inducing universities to raise tuition. Other questions revolve around whether the range of options and interactions among student loan

and grant programs make them hard to understand and challenging for students to calculate how best, when, and where to use them.<sup>5</sup>

Federal housing assistance offers another example of a major policy goal for which portfolio analysis could identify potential changes in strategy that would yield greater benefits and budget savings. GAO identified over 160 separate programs and activities assisting housing as shown in the following table.

**GAO Analysis of Housing Programs**

Primary purpose of activity*	Number of activities/programs	Agency/Entity															
		HUD	Treasury	USDA	FHFA	VA	Regulators	IRS	FFIEC	CFPB	FCS	Fannie	Freddie	FarmMk	Interior	Labor	FICA
Assistance for buying, selling, or financing a home	39	●	●	●	●	●											
Supports housing and other activities	30	●	●	●	●		●										
Assistance for financing rental housing	25	●	●	●	●												
Emergency assistance to housing market or current homeowner	16	●	●				●										
Regulatory requirements	10	●					●	●	●								
Increase availability of mortgage loans	9	●	●		●					●	●	●	●				
Assistance for homeowners	9	●	●		●									●			
Assistance for rental property owners	8	●	●														
Rental assistance for tenants	6	●	●												●		
Operation/management of rental housing	4	●	●														
Regulator of government-sponsored enterprises	2															●	●

CFPB = Consumer Financial Protection Bureau  
Fannie = Fannie Mae  
FarmerM = Federal Agricultural Mortgage Corporation (Farmer Mac)  
FCA = Farm Credit Administration  
FCS = Farm Credit System  
FFIEC = Federal Financial Institutions Examination Council  
FHFA = Federal Housing Finance Agency  
FHLM = Federal Home Loan Banks  
Freddie = Freddie Mac  
HUD = Department of Housing and Urban Development  
Interior = Department of Interior/Bureau of Indian Affairs

Labor = Department of Labor  
NRC = Neighborhood Reinvestment Corporation  
Regulators = Financial federal regulators include the Federal Reserve, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and National Credit Union Administration  
Treasury = Treasury  
USDA = Department of Agriculture  
VA = Department of Veterans Affairs

Source: GAO analysis of agency documentation.

Source: U.S. Government Accountability Office, *Housing Assistance: Opportunities Exist to Increase Collaboration and Consider Consolidation*, August, 2012, GAO-12-554

<sup>5</sup> U.S. Government Accountability Office, *Student Aid and Postsecondary Tax Preferences: Limited Research Exists on Effectiveness of Tools to Assist Students and Families Through Title IV and Tax Preferences* GAO-05-684, July, 2005

A specific focus on low income housing raises provocative questions with budgetary and performance implications. The budget includes about \$50 billion a year in various forms of low-income housing assistance. In 2014, this included \$37 billion in HUD subsidies to aid over 5 million low-income households (about 10 million people) – including residents of public housing and privately owned subsidized projects, and those renting private units with portable housing vouchers. Federal expenditures also included revenues losses for the Low-income Housing Tax Credit (LIHTC) used by States to develop new low-income housing projects, reducing federal revenues by \$ 7 billion in 2014. (It should be noted that these numbers are dwarfed by the over tax expenditures for homeownership, which reduced income tax revenues by \$130 billion in 2014.)

A portfolio analysis could consider the relative cost-effectiveness of these programs – and others administered by the Department of Agriculture and for homeless veterans by the Department of Veterans Affairs – used separately and in combination. Together, they constitute the current implicit federal strategy to improve housing and neighborhood conditions for low-income families and the elderly. They also, it should be noted, are part of a much broader set of programs to improve the lives and economic self-sufficiency of low-income people. Many questions have been raised about the best form and use of federal housing assistance, and new research suggests a potential for large gains by poor children if

their families use portable housing vouchers to relocate to neighborhoods where they can find better schools, greater safety, and better access to jobs.

Questions also could be asked about the best use of federal expenditures: for example, is it more cost-effective to subsidize construction of new projects, which in some places compete with older unsubsidized low-rent units and contribute to their abandonment, or to provide portable subsidies that allow more choice of housing type and location? Another set of questions concerns the characteristics and circumstances of those most likely to benefit from assistance: who should receive priority, and what other forms of assistance might enable them to get more benefit from a housing subsidy? A broader look at federal support for housing might ask whether, given the government's priorities and limited resources, support for homeownership – which mostly benefits more affluent people – could be reduced and the budget savings used to aid more modest-income households, whether renting or buying a first home.

These examples illustrate how a portfolio budgeting review may yield approaches to use limited resources more productively and to reduce fragmentation, overlap and duplication. Such options may include improved interagency coordination and strategic planning on the administrative side or program consolidation and redesign on the policy side. In some cases, such a review may conclude that fragmentation, on balance provides positive benefits by promoting increased choices to program beneficiaries and state and local governments.

While prompted by fiscal necessity, such deeper strategic reviews of the portfolio of major programs and policies for selected policy areas can serve the vital function of updating the federal government's programs and priorities. Many programs were, in fact, designed many years ago to respond to earlier concerns and priorities. We are reminded how much has changed in the past several decades from emerging shifts in security threats, globalization of economic transactions, changing environmental concerns, significant technological advances and aging populations. As the GAO said in a 2005 report, as we face continuing chronic and structural deficits, reexamining existing spending and tax programs may be the key to freeing up resources to address emerging needs.<sup>6</sup>

#### **Where Do We Go From Here?**

There are many pathways through which portfolio budgeting may take root in the budget process. The selection of areas for review and performance improvements could be accomplished in the Congress either by the leadership, in consultation with the President, or by this Committee as a part of the congressional budget process. The existing budget functions and subfunctions could be used as a basis for determining crosscutting policy areas, as intended when they were folded into the congressional budget process.

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<sup>6</sup> U.S. Government Accountability Office, *21<sup>st</sup> Century Challenges: Reexamining the Base of the Federal Government*, March, 2005, GAO-05-325SP

The budget committees can take the lead in fostering broad based portfolio reviews of major functions or subfunctions. They can do this on their own through task forces, similar to performance based reviews done by task forces of the Senate Budget Committee in the early 2000's. The Budget Committee also can do this by working collaboratively with authorizing and appropriations committees, commissioning portfolio reviews in concert with those committees.

Portfolio reviews can best serve the budget process if they were guided by a fiscal savings target. Such targets would ensure that the results would be used in budget formulation and help provide needed discipline to the selection of portfolio strategies and alternatives. Such reviews can be triggered by what we might call performance based reconciliation instructions where task forces or committees expected to report savings to be integrated by the budget committees into a reconciliation bill

The Executive Branch could be engaged in a collaborative effort to undertake a series of selective portfolio reviews. The President and Congress could reach agreement about those areas to be assessed in each budget year. Congress could advise the Administration that areas that are ripe for reexamination, such as those up for reauthorization, should get attention in the executive review process. Such a process would require the Congress to articulate its oversight and reexamination priorities centrally and the President to invite Congress to help determine priorities to guide the executive's own budget review process.



I don't need to tell this Committee that the performance assessment process I am suggesting will not be easy. There are no low hanging fruit in the federal budget. In fact, performance based assessments of the base of groups of programs will entail the prospect of greater conflict. This new role will require the Committee to gain the support of other leaders in the Congress as well as the Administration. It will be important for this process to be highly selective in its reviews, to avoid being overwhelmed by the sheer amount of work as well as the likely political reaction. Nonetheless, the potential rewards are substantial. Performance assessments carry the promise of transforming the budget process into a more strategic and forward looking vehicle for setting the nation's priorities.

Notwithstanding the challenges associated with reexamination, reviewing the base of programs and operations has ample precedent. The federal government, in fact, has reexamined and reformed selected programs and priorities in the past. From a programmatic perspective, such reexaminations have included, for example, the 1983 Social Security reform, the 1986 tax reform, and the 1996 welfare reform. They have also included reforms such as the creation of the Department of Homeland Security and, most recently, the ongoing reorganization of the U.S. intelligence community. From a broader fiscal standpoint, the 1990s featured significant deficit reduction measures adopted by the Congress and supported by the President that made important changes to discretionary spending, entitlement program growth, and revenues that helped eliminate deficits and bring about

budgetary surpluses. Roy Meyers indeed argues that budget reform is not necessarily an impossible political project, and shows examples such as earmark reform that seemed to defy the prevailing cynicism about Congressional resistance to new budget practices and institutions.<sup>7</sup>

Given CBO and GAO projections of unsustainable debt in years to come, Congress and the President will be called on to reach agreements to make hard choices to reduce spending and/or increase revenues. The question is whether such inevitable choices will be made through the regular process, supported by careful analysis and deliberation, using a method like portfolio budgeting, or whether they will be forged outside the regular order in the heat of a fiscal or economic crisis. I think we would all prefer the former.

#### **Conclusion: Transforming the Budget Committees**

Budget process reforms present risks and opportunities for the Congress and this Committee. The ideas for budget process reform I have laid out would place new demands on the federal budget process in general and this Committee in particular. I am well aware that these emerging roles are even more challenging for a Congress that has trouble simply passing a budget resolution and securing a full year's appropriations for the agencies. Yet the fiscal challenges and the need to update our

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<sup>7</sup> Roy Meyers, *The Political Feasibility of Doing What is Almost Impossible: Reforming the Federal Budget Process*, Working Paper for the National Budget Roundtable, George Mason University, September, 2015

priorities both call for major new activities that can best be performed by the Budget Committees.

Strengthening Congress' capacity to budget will call for stronger leadership within the Congress and from the President as well. This Committee will be challenged to assert a more proactive role in setting priorities, reviewing government performance and shifting how we budget for the long term. This is a tall order, particularly during today's period of polarized politics.

It may be time to rethink the nature of the budget committees. Established in 1974 as new committees alongside an established committee structure, the budget committees have increasingly been tasked to take on government-wide leadership without enough influence over other committees to do the job. Accordingly, some have suggested that budget committees be transformed into leadership committees, comprised of the chairs of the major committees of each house.<sup>8</sup>

An old adage in management suggests that form should follow function. The original design of the 1974 Budget Act contemplated a less ambitious role for the budget committees. Powerful committees were at hand to trim their sails. Yet over time, the budget process has had to adapt to serve new functions: reconciliation, new scoring rules implementing new budget legislation, and greater demand for complex

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<sup>8</sup> Philip G. Joyce, "Strengthening the Budget Committees: Institutional Reforms to Promote Fiscally Responsible Budgeting in Congress", paper prepared for the Federal Budget Reform Initiative, Pew Charitable Trusts, January, 2011.

analysis of long term and dynamic economic effects of proposed legislation have all changed the scope and stakes of the congressional budget process. The Budget Committees are at a threshold moment and need to adapt to meet the emerging needs of the Congress and the nation for a revitalized budget process.

Chairman ENZI. Thank you.  
Honorable McTigue from New Zealand.

**STATEMENT OF THE HONORABLE MAURICE P. MCTIGUE, VICE PRESIDENT FOR OUTREACH, MERCATUS CENTER, GEORGE MASON UNIVERSITY; FORMER CABINET MEMBER AND MEMBER OF PARLIAMENT, NEW ZEALAND; AND FORMER ADVISOR TO THE U.S. OFFICE OF MANAGEMENT AND BUDGET**

Mr. MCTIGUE. Good morning, Senator Enzi, and good morning, Senator Perdue. And, Senator Enzi, given your name, we may well be able to organize for you complimentary citizenship. [Laughter.]

I am honored to have been asked to testify before you today. The subject of this hearing is about the options for changing the budget process to produce better outcomes.

Two important themes immediately come to mind when considering budget process reform, and they are transparency and outcomes. This morning I will comment on three issues relevant to reforming budget processes: first, the effect of process change; budgeting to outcomes; and then overseas experiences.

Changing budget procedures can significantly change the incentives that members are subjected to as the budget process proceeds. Procedural change would be extremely effective if it was to institute a clear linkage between expenditure and outcomes. I applaud the passing this week of the new initiative on evidence-based policymaking. This is certainly a step in the right direction where decisions should be based upon evidence rather than on history.

Process changes will not bring about better budget outcomes on their own. Congress needs to make the hard decisions that are highlighted by a better budget process.

Government departments suffer from mission creep, and mission creep often is the cause of much duplication. Mission creep is a natural dynamic in organizations, and it leads to them spreading their activities outside from their core business.

With this mission creep, there is no rigorous comparison of the activities targeting the same outcome. That means that the budget is buying many services focused on the same outcome with varying results, varying costs, and probably denying the public an additional benefit that would come from investing in the best of those activities.

A good initiative would be to put a team of the best corporate restructuring specialists in the world into every department with the express purpose of returning each department to its core business and then shifting the inappropriate activity to where it belongs, or if it did not perform better than other activity, to terminate it. This is very much what Professor Posner has just recommended to you with his concept of portfolio budgeting.

Reforms within the legislature should restructure the budget accounts and the Budget Committees to align with sectors of the economy so that all decisions on a particular outcome are taken in the same place.

There should also be a consequence for not getting the budget done. My experiences in parliament and parliaments around the world, when you do not get the budget done, there is a new election immediately. That certainly means that budgets get done.

Speaking to outcomes, in 1993 Congress initiated a powerful reform with the Government Performance and Results Act. The purpose of that law was for governments to make budget decisions based on results or outcomes. At the Mercatus Center, we evaluated every one of those reports from the 24 major departments for the first 10 years of GPRA, and we ranked them according to the quality of their results disclosure. By the end of that period, departments were producing good, actionable information on their effect on public outcomes. The sad fact is that performance information did not become a tool of the appropriation process. The return of departments to their core business would greatly aid results accountability.

Looking at overseas trends, many countries overseas have in recent years tried to define “fiscally responsible behavior” and have then legislated to embed that definition in law. The definition differs by country, but the intent is the same in every case, and that is, to rein in irresponsible spending and taxing and to make transparent to the people the behavior of their governments.

In most instances, the reform of these countries separates the budget strategy and policy from the budget numbers documents by releasing a strategy and policy document some 6 months ahead of the budget numbers document, allowing comment on strategy and decisions on strategy and policy before the numbers come before the legislature. This process, while retaining annual budgeting, produces 3- to 4 year out-numbers that are firm so there is greater certainty about medium-term spending.

The most dramatic example right now of the effect of fiscally responsible behavior is in Brazil where the current president is under impeachment for having breached the fiscal responsibility law of Brazil. Her breach was that she understated the deficit that the nation would face. That certainly is bringing a consequence to the process.

The other case of interest is Ireland where their fiscal responsibility law sets up the independent Irish Fiscal Advisory Council. The council’s job is to comment publicly on whether the government is acting in a fiscally responsible manner.

In the case of my own country, New Zealand, after the passage of the Fiscal Responsibility Act of 1994, the government went from 23 years of deficits to 16 years of surpluses. For those countries that have tackled the challenge of being accountable for fiscally responsible behavior, there seems to be a change in culture.

Mr. Chairman and members of the Committee, I applaud the work that you are doing, the initiative in attempting to reform budget procedures, because the evidence shows that much good can come from such an initiative.

Thank you.

[The prepared statement of Mr. McTigue follows:]



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## TESTIMONY

### CAN BUDGET PROCESS REFORMS PRODUCE BETTER BUDGET OUTCOMES?

**HON. MAURICE P. MCTIGUE, QSO**

*Vice President for Outreach, Mercatus Center at George Mason University*

Senate Committee on the Budget

Hearing: Fixing the Broken Budget Process: Outcome Budgeting to Maximize Taxpayer Value

April 13, 2016

Chairman Enzi and Ranking Member Sanders, I am honored to have been invited to testify before you on process and procedural options for reforming the budget process.

I am a vice president at the Mercatus Center at George Mason University. My work there over the last 15 years has focused on mechanisms that would improve the quality of governance in America. Prior to this, I served as an elected member of the New Zealand Parliament and a member of the Cabinet of New Zealand, and was then appointed New Zealand's ambassador to Canada. The New Zealand government implemented a series of reforms to budget procedures when I served as a legislator. Canada made major changes to its budget processes during my tenure there. My comments today will draw on my research, as well as these experiences, and on research that we have done at the Mercatus Center on budget procedures throughout the United States.

Today I will comment on “wasteful and duplicative spending,” and discuss how better, more transparent budget processes are the first step, but not the solution, to controlling such spending. I would like to make three main points. First, changing the focus to the desired outcomes in the budget process is essential to controlling duplicative spending. Second, comparing the results of all activities that impact the same outcome is critical in allocating resources to the most effective activities and maximizing outcome achievement. And third, budget procedures matter when it comes to controlling spending, based on evidence from state governments and overseas.

#### US EFFORTS IN IMPROVING PERFORMANCE INFORMATION TO INFORM SPENDING LEVELS

Over the last 25 years, many national, state, and provincial governments have experimented with changes to their budget processes and procedures—with varying levels of success. In nearly every case the objective of the reforms has been to develop a closer relationship between the outcomes of government spending and future

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*The ideas presented in this document do not represent official positions of the Mercatus Center or George Mason University.*

appropriation decisions. While there are many instances where government agencies have significantly improved their ability to produce quality, outcome-oriented performance information, the initiatives have frequently stumbled at the spending decisions made by legislatures.

Not the least of these frustrations was the American experience with the Government Performance and Results Act (GPRA) and its later iterations. Mercatus conducted an annual evaluation of the Annual Reports of the 24 Chief Financial Officers Act agencies for the first 10 years of GPRA.<sup>1</sup> In the initial years Annual Reports produced very poor quality performance information. But at the end of the 10 years, all agencies had dramatically improved the quality and the clarity of their reporting, with some agencies consistently producing excellent reports. The disappointing finding with the evaluation of 10 years of the Annual Reports was that this quality performance information was hardly ever used to inform the appropriations process. So changed procedures will not, on their own, improve budget decision-making if the legislature does not change its practices as well. However, better budget processes that more starkly demonstrate the options available to appropriators—and the consequences of each of the options—may well change the incentives for appropriators.

#### CONTROLLING DUPLICATIVE SPENDING BY FOCUSING ON OUTCOMES

Successfully limiting duplicative and wasteful spending requires a change in the thought process behind budget decision-making. This means moving away from funding an activity or program and instead focusing on funding the outcome desired by policymakers. It is this concept that led the New Zealand Parliament to reorganize its committees and change the Financial Reporting Act so that parliamentary select committees had direct oversight of sectors of the economy instead of departments and programs. Under this new arrangement the Education and Science Committee examined all activity that was focused on education, regardless of which agency delivered the program. Under this arrangement the committee oversaw all education programs, could identify which were the most effective, which were the least effective, and how much each cost per unit of success. This enabled appropriators to strategically allocate resources to achieve the greatest public benefit. Parliament was able to eliminate outdated and redundant activity.

To shift the budget focus to outcome achievement, appropriations in New Zealand are now converted to purchase agreements that spell out precisely what the government expects in outcome results for this investment. For example; this investment of \$XXX will buy an increase of 10 percent in ten-year-olds who are reading at their biological age. The purchase agreement is a binding contract between the CEO of the agency and the government. Failure to deliver the commitments in the contract could lead to the termination of the CEO's employment.

Wasteful and duplicative expenditure is best controlled by ensuring that all activities addressing a common outcome have to compete for a common pool of money in the appropriations process. Reorganizing existing budget accounts by mission or objective could help policymakers and the public better relate costs to results.

#### GETTING SPENDING UNDER CONTROL: EXPERIENCE IN THE STATES

Research conducted by Matt Mitchell and Nick Tuszynski and published by the Mercatus Center examined differing budget procedures across the 50 states.<sup>2</sup> (The study is attached to this testimony as an appendix.) They found that different budget procedures had a significant effect on per capita spending in the state concerned, as demonstrated in the example below and in figure 1.

1. See Jerry Ellig, "Ten Years of Results from the Results Act" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, May 2010); and Annual Performance Report Scorecards, Mercatus Center at George Mason University, <http://mercatus.org/all-publications/scorecard>.

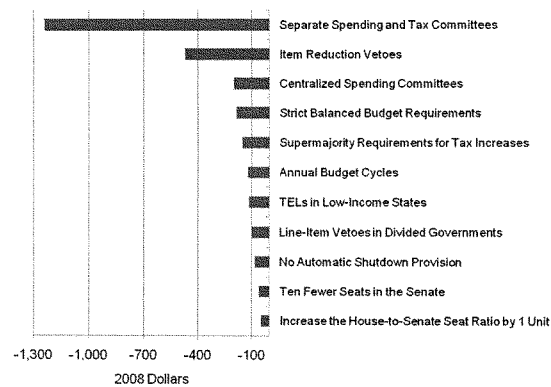
2. Matthew D. Mitchell and Nick Tuszynski, "Institutions and State Spending: An Overview" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, October 2011).



Merely having different committees that consider taxing and expenditure separately reduces per capita spending by \$1,241. And having a line item reduction authority reduces spending by \$471 per capita. To put these figures in perspective, 2008 state and local per capita expenditures averaged approximately \$5,708.<sup>3</sup>

Thus, the studies we review suggest that these institutions can decrease per capita spending up to 22 percent. It is clear that Justice Brandeis's "experiment" has yielded economically significant results.

Figure 1: The Marginal Impact of Institutions on Per Capita Spending



Sources: Separate Committees: Crain and Muris, 1995; Item Reduction Vetoes: Crain, 2003; Centralized Spending Committees: Crain and Muris, 1995; Strict Balanced Budget Requirements: Primo, 2003; Supermajority Requirements for Tax Increases: Crain, 2003; Annual Budget Cycles: Crain, 2003; TELs in Low-Income States: Crain, 2003; Line-Item Vetoes in Divided Government: Besley and Case, 2003; Shutdown Provisions: Primo, 2007; Senate Seats: Gilligan and Matsusaka, 1995; House-to-Senate Ratio: Chen and Malhotra, 2007. The authors have converted all figures into 2008 dollars.

## OVERSEAS TRENDS

Governments in other countries, driven by dissatisfaction with outcomes from existing practices, have been debating and legislating different budget procedures.

Many are starting the budget process early by separating budget policy and economic strategy from spending by publishing a budget policy and strategy document as many as six months before the budget. The goal is to allow extensive debate on these issues prior to the appropriation process.

Some have shortened the time for the appropriation process (New Zealand's is only 12 weeks) since many of the contentious issues have already been debated. As each of these countries has a parliamentary system, the consequence for not passing the budget is an immediate new election.

There is a trend to much greater transparency throughout these new procedures, and they have developed statutes that make it more difficult for governments to depart from established procedures and requirements. Some, like

3. Updated research that independently tested the effect of separate taxing and spending committees confirmed that states with separate taxing and spending committees are associated with less spending—much less than most other institutions. Matthew D. Mitchell and Pavel A. Yakolev, "A House Divided Against Itself Cannot Spend (as Much): The Fiscal Effect of Separate Taxing and Spending Committees in State Legislatures" (Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, May 2015).

Ireland, have set up independent bodies to comment on how well the government is meeting fiscal and budget requirements.

The following are summaries of laws from different countries that give a picture of some initiatives. (Appendix I gives more detail on each of the laws referenced.)

Australia: the Charter of Budget Honesty Act 1998.<sup>4</sup> This was the Australian response to the frustration felt by incoming governments that the country's fiscal position after an election was often much worse than had been portrayed during the election.

Ireland: the Fiscal Responsibility Act.<sup>5</sup> This was a response to the perceived fiscal nonaccountability of successive governments. This law did something extraordinary—it set up the statutorily independent Irish Fiscal Advisory Council. The council's job, as laid out in the statute, is to comment quite specifically on whether the government is acting in a fiscally responsible manner.

New Zealand: the Fiscal Responsibility Act and the Financial Reporting Act.<sup>6</sup> These laws, and a number of others, were responses to decades of highly inept fiscal management that led the country to the verge of bankruptcy in the early 1980's. "Having cleaned up the mess, don't let it happen again" probably best describes the rationale driving the compendium of fiscal and operational laws passed in New Zealand.

## CONCLUSION

There exists a huge volume of research and real world experience, both in the United States and overseas, on the subject of budget processes and procedures. My testimony has touched very lightly on a number of the initiatives currently in practice to identify options that might be attractive to the Senate. What can be said with certainty is that more transparent procedures, a linkage between agency performance and future budget allocations, and a focus on measuring progress against outcome achievements all appear to be goals of these initiatives. It could also be said that there appears to be a cultural shift within these nations to a greater appreciation of the importance of keeping spending and debt within predetermined parameters that define fiscally responsible behavior.

4. *Charter of Budget Honesty Act 1998* (Australia), <https://www.legislation.gov.au/Series/C2004A05333>.

5. *Fiscal Responsibility Act 2012* (Republic of Ireland), <http://www.fiscalcouncil.ie/fiscal-responsibility-act/>.

6. *Fiscal Responsibility Act 1994* (New Zealand), <http://www.treasury.govt.nz/publications/research-policy/wp/2001/01-25/04.htm>; *Financial Reporting Act 1993* (New Zealand), <http://www.treasury.govt.nz/economy/overview/2010/23.htm>.

## APPENDIX I

Australia: Charter of Budget Honesty Act 1998<sup>7</sup>

The *Charter of Budget Honesty Act 1998* (the Charter) sets out principles and requirements that guide the government's management of fiscal policy. The Charter requires the government to:

- set out its medium-term fiscal strategy, along with its shorter-term fiscal objectives and targets, which are published in the Budget Papers and in the MYEFO report
- report on estimates for the General Government Sector (GGS) according to an annual reporting cycle, including economic assumptions underlying Budget estimates
- report against specified external reporting standards
- list all proposals for changes to revenue, current and capital expenditure in the forthcoming reporting cycle.

Ireland: Fiscal Responsibility Act<sup>8</sup>

The Fiscal Responsibility Act came into effect in December 2012. The introduction of the Act was part of a wider agenda of budgetary reform, benchmarked under the Programme for Government 2011 and the EU/IMF Programme of Financial Support for Ireland.

The Act established the Irish Fiscal Advisory Council as a statutory body and legislated for the implementation of national and EU fiscal rules. Further EU regulations (July 2013) resulted in the Council being assigned the role of the independent body that would endorse the macroeconomic forecasts produced by the Department of Finance on which Budgets and Stability Programmes are based (implemented by Ministers and Secretaries Amendment Act 2013). The process of this additional function is outlined in the Memorandum of Understanding (signed version) between the Council and the Department of Finance.

Under the Fiscal Responsibility Act the mandate of the Irish Fiscal Advisory Council is:

- To endorse, as it considers appropriate, the macroeconomic forecast prepared by the Department of Finance on which the Budget and Stability Programme Update are based.
- To assess the official forecasts produced by the Department of Finance. These are the macroeconomic and budgetary forecasts published by the Department twice a year.
- To assess whether the fiscal stance of the Government is conducive to prudent economic and budgetary management, with reference to the EU Stability and Growth Pact.
- To monitor and assess compliance with the budgetary rule as set out in the Fiscal Responsibility Act. The budgetary rule requires that the Government's budget is in surplus or in balance, or is moving at a satisfactory pace towards that position.
- In relation to the budgetary rule, to assess whether any non-compliance is a result of 'exceptional circumstances'. This could mean a severe economic downturn and/or an unusual event outside the control of Government which may have a major impact on the budgetary position.

The Acts ensure the independence of the Council in the operation of its functions.

7. Australian Government Department of Finance, "Budget Process," June 15, 2015.

8. Irish Fiscal Advisory Council, "Fiscal Responsibility Act," accessed April 7, 2016.

New Zealand: The Fiscal Responsibility Act 1994<sup>9</sup>

The FRA aims to improve fiscal policy by specifying principles of responsible fiscal management and strengthening reporting requirements.

### 3.1 Principles of responsible fiscal management

- a. Governments are required to follow a legislated set of principles and publicly assess their fiscal policies against these principles. Governments may depart temporarily from the principles but must do so publicly, explain why they have departed, and indicate how and when they intend to conform to the principles. The five principles of responsible fiscal management are: Reducing total Crown debt to prudent levels so as to provide a buffer against factors that may impact adversely on the level of total Crown debt in the future, by ensuring that, until such levels have been achieved, the total operating expenses of the Crown in each financial year are less than its total operating revenues in the same financial year.
- b. Once prudent levels of total Crown debt have been achieved, maintaining these levels by ensuring that, on average, over a reasonable period of time, the total operating expenses of the Crown do not exceed its total operating revenues.
- c. Achieving and maintaining levels of Crown net worth that provide a buffer against factors that may impact adversely on the Crown's net worth in the future.
- d. Managing prudently the fiscal risks facing the Crown.
- e. Pursuing policies that are consistent with a reasonable degree of predictability about the level and stability of tax rates for future years.

Definitions such as "prudent" level of debt, or "reasonable" degree of predictability are not specified in the Act. It is left to the Government of the day to interpret the relevant fiscal terms.

Importantly, although a Government can depart from the principles, the FRA requires any such departure to be temporary and that the Minister of Finance specify the reasons for departure, the approach to be taken to return to the principles and the period of time this is expected to take.

### 3.2 Reporting requirements

Governments must publish a Budget Policy Statement (BPS) before the annual Budget and a Fiscal Strategy Report (FSR) at the time of the Budget (see Box 1). These publications must demonstrate the consistency of the Government's short-term fiscal intentions and long-term fiscal objectives with the principles of responsible fiscal management (Table 1 provides more detail). The Act requires the FSR to include fiscal projections (the "Progress Outlooks") covering a minimum of 10 years for the variables specified as long-term fiscal objectives.

The Treasury is required to prepare regular economic and fiscal forecasts (see Box 1). Having the timing and broad nature of the overall forecasts specified in legislation raises their credibility.

Under the FRA, all financial statements included in reports required by the Act are prepared under Generally Accepted Accounting Practice (GAAP). Fiscal reporting follows a set of consistent accounting rules established independently by the Accounting Standards Review Board (which sets accounting standards that are mandatory for both the public and private sector). The use of accrual accounts means that the full cost of policy must be disclosed, including non-cash items like depreciation and changes to government employee pension rights. The predecessor of GAAP was "Table 2" which was prepared on a cash basis.

9. John Janssen, "New Zealand's Fiscal Policy Framework: Experience and Evolution" (Treasury Working Paper 01/25, New Zealand Treasury), 9-10.

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# **WORKING PAPER**

## **INSTITUTIONS AND STATE SPENDING: AN OVERVIEW**

By Matthew Mitchell and Nick Tuszynski

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The ideas presented in this research are the authors' and do not represent official positions of the Mercatus Center at George Mason University.

## Institutions and State Spending: An Overview

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Matthew Mitchell and Nick Tuszynski<sup>1</sup>

### Abstract

U.S. fiscal policy at the federal, state, and local level is on an unsustainable path. While reformers should look for ways to reduce spending on particular budget items, tomorrow's legislatures may easily reverse these cuts. In contrast, a change in the rules that govern the political process—the “institutions” that shape a budget—can have a lasting effect on spending for years to come. Codified in statutes and in constitutions, these institutions include the rules of budgeting, electioneering, and legislating. They influence the decisions of legislators, governors, presidents, bureaucrats, voters, and even lobbyists. As such, institutional reform can be a more effective and sustainable path to fiscal probity than a one-time budget cut. This paper summarizes the empirical investigations of sixteen state-level institutions. The lesson for both state and federal policy makers is that there are a number of institutional reforms that seem likely to put spending on a more sustainable path.

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<sup>1</sup> We thank Meg Patrick for excellent research assistance and Jennifer Zambone and Emma Elliott for superb editorial improvements.

## Introduction

U.S. fiscal policy at the federal, state, and local level is on an unsustainable path.<sup>2</sup> While reformers should look for ways to reduce spending on particular budget items, tomorrow's legislatures may easily reverse these cuts. In contrast, a change in the rules that govern the political process—the “institutions” that shape a budget—can have a lasting effect on spending for years to come.<sup>3</sup> Codified in statutes and in constitutions, these institutions include the rules of budgeting, electioneering, and legislating. They influence the decisions of legislators, governors, presidents, bureaucrats, voters, and even lobbyists. As such, institutional reform can be a more effective and sustainable path to fiscal probity than a one-time budget cut.

Justice Brandeis famously referred to the federal system as a “laboratory” in which each state was free to implement novel social and economic experiments.<sup>4</sup> For the social scientist interested in understanding how institutions affect policy outcomes, the metaphor is apt. Each of the 50 states has its own set of institutions and some of these have changed over the course of the last several decades. At the same time, many other factors that might influence outcomes are invariant across the states. In other words, cross-state studies effectively control for factors such as macroeconomic conditions, culture, and the broad legal/constitutional setting in which each state operates. Moreover, researchers are able to employ various econometric techniques to control for the influence of those factors that *are* different across states such as climate or demography. In sum, the setting provides a rich laboratory in which to test the effect of different institutions on spending.

A large number of researchers have performed these tests and this paper reviews this literature, summarizing the effect of more than a dozen institutions on state spending.<sup>5</sup> This paper concentrates on peer-reviewed studies that rely on large data sets and well-accepted econometric techniques. Each of these studies carefully accounts for other factors that have been shown to impact spending such as demography, climate, and the economy.

This paper begins with some of the most-studied institutions, e.g., strict balanced budget requirements, move on to those that have received comparatively less attention, e.g., item-reduction vetoes, and

<sup>2</sup> For past state spending, see Matthew Mitchell, “State Spending Restraint: An Analysis of the Path Not Taken,” (working paper, Mercatus Center at George Mason University, Arlington, VA, 2010), [http://mercatus.org/sites/default/files/publication/State%20Spending%20Restraint%20An%20Analysis%20of%20the%20Path%20Not%20Taken%20corrected.%2010.1.10\\_0.pdf](http://mercatus.org/sites/default/files/publication/State%20Spending%20Restraint%20An%20Analysis%20of%20the%20Path%20Not%20Taken%20corrected.%2010.1.10_0.pdf). For future state spending, see Jeffrey Miron, “The Fiscal Health of U.S. States,” (working paper, Mercatus Center at George Mason University, Arlington, VA, 2011), [http://mercatus.org/sites/default/files/publication/State%20Spending%20Restraint%20An%20Analysis%20of%20the%20Path%20Not%20Taken%20corrected.%2010.1.10\\_0.pdf](http://mercatus.org/sites/default/files/publication/State%20Spending%20Restraint%20An%20Analysis%20of%20the%20Path%20Not%20Taken%20corrected.%2010.1.10_0.pdf). For future federal spending, see Congressional Budget Office, *Long Term Budget Outlook* (Washington, DC, June 2011), <http://www.cbo.gov/doc.cfm?index=12212>.

<sup>3</sup> The Nobel Laureate Douglass North is often considered the father of modern institutional economics. In his terms, institutions “are the humanly devised constraints that shape human interaction.” Douglass North, *Institutions, Institutional Change and Economic Performance* (New York: Cambridge University Press, 1990).

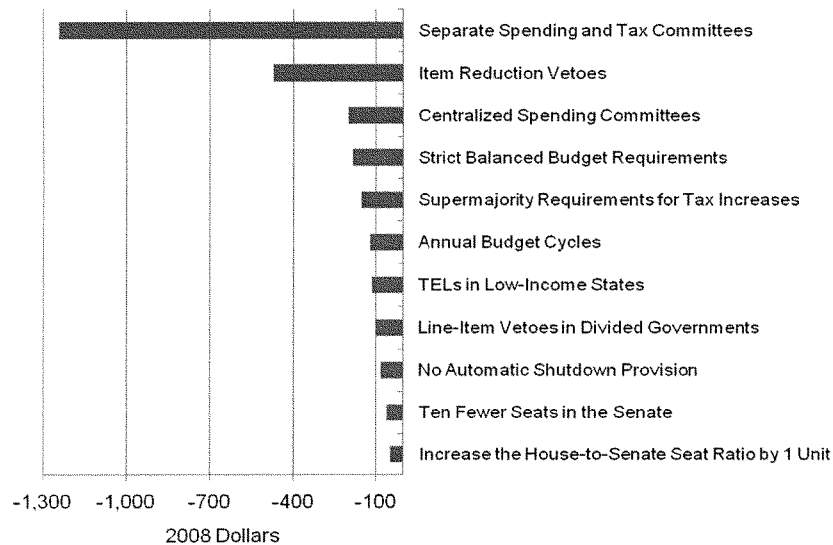
<sup>4</sup> *New State Ice Co. v. Liebmann*, 285 U.S. 262 (1932), <http://caselaw.lp.findlaw.com/scripts/getcase.pl?court=us&vol=285&invol=262>.

<sup>5</sup> Though this paper focuses on the effect of institutions on spending, there is a larger literature focusing on the effect of institutions on a wide variety of policy outcomes. For a review of this larger literature, see Timothy Besley and Anne Case, “Political Institutions and Policy Choices: Evidence from the United States,” *Journal of Economic Literature*, Vol. 41, No. 1 (March, 2003), 7-73, <http://www.jstor.org/pss/3217387>.

concludes with a pair of institutions, the study of which has yielded conflicting conclusions, e.g., direct democracy and term limits. Where possible, this paper presents the findings in terms of the institutions' impact on per capita spending and convert all numbers into 2008 dollars to permit side-by-side comparison. Our hope is that this overview will provide useful insights to state policy makers who may be interested in reform. We also hope it will be helpful to federal policy makers since many of these institutions may be transferred to the federal level.

Figure 1 highlights the results of those studies that present their findings in terms of per capita spending. To put some of these figures in perspective, 2008 state and local per capita expenditures averaged approximately \$5,708.<sup>6</sup> Thus, the studies we review suggest that these institutions can decrease per capita spending anywhere from 1 percent to 22 percent. It is clear that Justice Brandeis's "experiment" has yielded economically significant results.

Figure 1: The Marginal Impact of Institutions on Per Capita Spending



Sources: Separate Committees: Crain and Muris, 1995; Item Reduction Vetoes: Crain, 2003; Centralized Spending Committees: Crain and Muris, 1995; Strict Balanced Budget Requirements: Primo, 2003; Supermajority Requirements for Tax Increases: Crain, 2003; Annual Budget Cycles: Crain, 2003; TELs in Low-Income States: Crain, 2003; Line-Item Vetoes in Divided Government: Besley and Case, 2003; Shutdown Provisions: Primo, 2007; Senate Seats: Gilligan and Matsusaka, 1995; House-to-Senate Ratio: Chen and Malhotra, 2007. The authors have converted all figures into 2008 dollars.

<sup>6</sup> Authors' calculation. State Government Finances, *U.S. Census Bureau* (2010), [http://www.census.gov/govs/state/historical\\_data\\_2008.html](http://www.census.gov/govs/state/historical_data_2008.html) and *Population Estimates*, U.S. Census Bureau (2010), <http://www.census.gov/popest/eval-estimates/eval-est2010.html>.



## Sixteen Institutions and Their Effects on State Spending

### 1. *Strict Balanced Budget Requirements*

With the exception of Vermont, every state has a balanced budget requirement, but the stringency of these requirements varies widely. For example, in some states, the governor must submit a balanced budget, but the legislature need not pass one. In other states, estimates of the enacted budget need to show balance, but there are no consequences if these estimates prove wrong at the end of the fiscal year and the actual budget is out-of-balance. In some states, the legislature may carry-over a deficit from one year to the next, while in others they may not. Lastly, in some states an independently elected Supreme Court is the ultimate enforcer of the requirement, while in others the legislature appoints the members of the Supreme Court.

Even though balanced budget requirements are designed to ensure only that spending be less than revenue, there is reason to believe these requirements may reduce *both* spending and revenue. The Nobel laureate James Buchanan and his coauthor Richard Wagner explained why this might be when they observed that the ability to buy items for current voters while leaving future voters to pick up the tab systematically biases policy in favor of greater spending.<sup>7</sup>

Indeed, a number of studies have found that states with stricter balanced budget requirements tend to tax and spend less than other states. Henning Bohn of U.C. Santa Barbara and Robert Inman of the University of Pennsylvania, for example, find that per capita spending is about \$189 less in states with strict balanced budget requirements relative to those with only weak requirements.<sup>8</sup> David Primo of the University of Rochester arrives at a remarkably similar result, finding that strict balanced budget requirements reduce per capita spending by about \$184 per capita.<sup>9</sup> If this is the impact of moving from a weak to a strict balanced budget requirement, it is possible that if the federal government were to adopt a balanced budget requirement where none now exists then the impact would be even greater.

Strict balanced budget requirements have other salubrious effects. Bohn and Inman also find that states with strict requirements tend to have larger rainy day funds and larger surpluses and that states with these requirements tend to balance their books through spending reductions rather than revenue increases. Shanna Rose of New York University finds that states without strict balanced budget requirements are more likely to suffer from a “political business cycle” whereby policy makers increase spending just prior to an election, only to cut back following the election.<sup>10</sup>

<sup>7</sup> James Buchanan and Richard Wagner, *Democracy in Deficit: The Political Legacy of Lord Keynes* (Indianapolis: Liberty Fund, [1977] 1999).

<sup>8</sup> This estimate, like all others reported in this paper, has been converted into 2008 dollars for ease of comparison. When authors report a range of estimates, we have taken the average and then converted that average into 2008 dollars. Henning Bohn and Robert Inman, “Balanced Budget Rules and Public Deficits: Evidence from the U.S. States” (working paper No. 5533, National Bureau of Economic Research, 1996).

<sup>9</sup> David Primo, *Rules and Restraint: Government Spending and The Design of Institutions* (Chicago: University of Chicago Press, 2003). Mark Crain has also corroborated this result. See Mark Crain, *Volatile States: Institutions, Policy and the Performance of American State Economies* (Ann Arbor: University of Michigan Press, 2003).

<sup>10</sup> Shanna Rose, “Do Fiscal Rules Dampen the Political Business Cycle?” *Public Choice* 128, no.3/4 (2006): 407-31.

But there may be some unintended consequences of a strict balanced budget requirement. Economists Noel Johnson, Matthew Mitchell, and Steven Yamarik recently concluded that while such rules limit the likelihood of partisan fiscal outcomes, they increase the likelihood of partisan regulatory outcomes. When Democratic-controlled states were unable to carry a deficit forward to the next fiscal cycle, they were more likely to raise the minimum wage, less likely to adopt a right-to-work statute, and more likely to regulate personal freedoms.<sup>11</sup>

## 2. State Rainy Day Funds

Some commentators worry that a balanced budget requirement exacerbates the ups and downs of the business cycle. Since state budgets tend to be the tightest at the bottom of an economic downturn, this argument goes, strict balanced budget requirements force states to cut back on spending at the worst time.<sup>12</sup> One institutional answer to this critique is a “budget stabilization fund,” better known as a rainy day fund. States contribute to these funds during good years and then draw on them when the budget is strained due to a downturn or some other event such as a natural disaster. Forty-seven states currently maintain such funds, but like many institutions, their design varies on a state-by-state basis.<sup>13</sup>

Studies of rainy day funds suggest that they can smooth out the spending-cycle, but the details matter. Gary Wagner of Duquesne University and Erick Elder of the University of Arkansas conducted the most-comprehensive recent study of rainy day funds. They find that states whose rainy day funds have strict rules governing deposits and withdrawals tend to experience a \$14 per capita reduction in spending volatility (as measured by the cyclical variability of per capita spending over time).<sup>14</sup>

## 3. Supermajority Requirements for Tax Increases

Fifteen states require supermajority votes of the state legislature to raise taxes.<sup>15</sup> Depending on the state, these rules require two-thirds, three-fourths, or three-fifths of the legislature to consent to a tax increase. In some states, the supermajority requirement applies to all taxes and in others it applies to a subset of taxes. A number of researchers have found that these rules reduce spending. Economists Mark Crain and James Miller III, for example, find that states with supermajority requirements for tax increases tend to increase spending at a slower pace.<sup>16</sup> A subsequent study by Brian Knight of Brown University finds that the effective tax rate in states with these requirements is between 8 and 23 percentage points lower than in states without such a requirement.<sup>17</sup> The latest and most-comprehensive studies suggest that these

<sup>11</sup> Noel Johnson, Matthew Mitchell, and Steven Yamarik. “Pick Your Poison: Do Politicians Regulate When they Can’t Spend?” (working paper, Mercatus Center at George Mason University, Arlington, VA, 2011), [http://mercatus.org/sites/default/files/publication/Partisan\\_Policies\\_Johnson\\_Mitchell\\_Yamarik\\_WP1128\\_0.pdf](http://mercatus.org/sites/default/files/publication/Partisan_Policies_Johnson_Mitchell_Yamarik_WP1128_0.pdf).

<sup>12</sup> Norman Ornstein, “Why a Balanced-Budget Amendment is Too Risky,” *Washington Post*, July 29, 2011, <http://www.aei.org/article/103883>.

<sup>13</sup> Kim Rueben and Carol Rosenberg, “State and Local Tax Policy: What Are Rainy Day Funds and How Do They Work?” in *The Tax Policy Briefing Book*, Tax Policy Center, August 12, 2009, <http://www.taxpolicycenter.org/briefing-book/state-local/fiscal/rainy-day.cfm>.

<sup>14</sup> Gary Wagner and Erick Elder, “The role of Budget Stabilization Funds in Smoothing Government Expenditures Over the Business Cycle,” *Public Finance Review*, Vol. 33, No. 4 (July 2005): 439-65.

<sup>15</sup> Bert Waisanen, “State Tax and Expenditure Limits—2010,” National Conference of State Legislatures, 2010.

<sup>16</sup> Mark Crain and James Miller III, “Budget Process and Spending Growth,” *William and Mary Law Review*, Vol. 3, No. 4 (1990): 1021-46.

<sup>17</sup> Brian Knight, “Supermajority Voting Requirements for Tax Increases: Evidence from the States,” *Journal of Public Economics*, Vol. 76, No. 1 (2000): 41-67. An effective tax rate is the percent of income that an average citizen pays in taxes.

requirements are associated with significantly lower per capita spending levels. Crain, for example, finds that states with these rules spend, on average, \$151 less per capita.<sup>18</sup> Similarly, economists Timothy Besley and Anne Case find that these rules reduce per capita spending by \$103.<sup>19</sup>

#### 4. Tax and Expenditure Limits

In the last several decades, a number of states have experimented with formal rules that are specifically designed to arrest the rate of growth of government. These so-called “tax and expenditure limits” (TELs) are either codified in the statutes or constitutions of 28 states.<sup>20</sup> The rules bind state spending, taxation, or both through formulas that reference factors such as the personal income of state residents, population growth, the inflation rate, or some combination thereof.

Early studies of these rules concluded that they generally fail to restrain the fiscal growth of government.<sup>21</sup> Newer studies, though, use larger and more detailed data sets and tend to find that these institutions can be effective in certain circumstances.<sup>22</sup> As with balanced budget requirements and rainy day funds, however, the details matter.

A number of studies, noting that TEL formulas are often based on residents’ incomes, examine whether TELs have different effects in high versus low-income states. Crain, for example, finds that TELs in low-income states seem to reduce spending by about \$114 per capita while TELs in high-income states seem to increase spending by about \$534 per capita.<sup>23</sup>

Other studies have focused on the fact that the details of TEL laws vary considerably from state to state. These, too, have tended to conclude that TELs can effectively restrain spending, but only in certain circumstances. Mitchell, for example, found that TELs are more effective when their formula is based on the sum of inflation plus population growth, when they bind spending rather than revenue, when they require a supermajority rather than a simple majority vote to be overridden, when they immediately refund revenue collected in excess of the limit, and when they prohibit unfunded mandates on local governments.<sup>24</sup>

<sup>18</sup> Crain, *Volatile States: Institutions, Policy and the Performance of American State Economies*.

<sup>19</sup> Besley and Case, “Political Institutions and Policy Choices: Evidence from the United States.”

<sup>20</sup> Waisanen.

<sup>21</sup> See, for example, Burton Abrams and William Dougan, “The Effects of Constitutional Restraints on Government Spending,” *Public Choice*, Vol. 49 (1986): 101-16.

<sup>22</sup> This is not always true, however. One recent study found TELs to be “largely ineffective.” Thad Kousser, Matthew McCubbins, and Ellen Moule, “For whom the TEL Tolls: Can State Tax and Expenditure Limits Effectively Reduce Spending?” *State Politics and Policy Quarterly*, Vol. 8 (2008): 331-61.

<sup>23</sup> Crain, *Volatile States: Institutions, Policy and the Performance of American State Economies*. Crain defines low and high-income states as those whose incomes are one standard deviation above or below the mean. Similar findings were obtained by Ronald Shadbegian, “Do Tax and Expenditure Limitations Affect the Size and Growth of State Government?” *Contemporary Economic Policy*, Vol. 14 (1996): 22-35, and by Matthew Mitchell, “TEL It Like It Is: Do State Tax and Expenditure Limits Actually Limit Spending?” (working paper, Mercatus Center at George Mason University, Arlington, VA, 2010), <http://mercatus.org/sites/default/files/publication/TEL%20It%20Like%20It%20Is.Mitchell.12.6.10.pdf>.

<sup>24</sup> Mitchell, “TEL It Like It Is: Do State Tax and Expenditure Limits Actually Limit Spending?”

### 5. Line-item Vetoes

Like the president of the United States, every governor in the union possesses a veto power. In addition to the simple veto, however, 44 governors possess a “line-item veto.” This allows them to strike specific sections from a bill.<sup>25</sup> At the federal level, a statutory line-item veto was approved by both houses of the Congress and signed by President Clinton in 1996. In 1998, however, the Supreme Court struck down the law.<sup>26</sup> Now, a federal line item veto would either require constitutional amendment, or a carefully-worded statute that ensured the legislative branch retained the final say on the matter.<sup>27</sup>

Early studies of the line-item veto at the state level found that it had no impact on overall state spending.<sup>28</sup> Subsequent research, however, has focused on the impact of the line-item veto in times and places where different parties control the governor’s mansion and the legislature.<sup>29</sup> This line of research has found that the line-item veto can have a large and statistically significant impact on per capita spending. Besley and Case, for example, find that in a state with a divided government the line-item veto reduces per capita spending by about \$100.<sup>30</sup>

### 6. Item-reduction Vetoes

In most cases, when a governor possesses a line-item veto, he must completely defund any budget items he wishes to strike. In twelve states, however, the governor need not zero-out the entire item.<sup>31</sup> Instead, he may write in a lower amount. In such cases, the governor is said to possess an “item-reduction veto.” Theoretically, an item-reduction veto changes the negotiating power between the governor and the legislature by effectively denying the legislature the ability to make the governor a take-it-or-leave-it offer. Mark Crain estimates that this particular variety of veto seems to have a substantial effect on spending, lowering per capita expenditures by \$471.<sup>32</sup>

### 7. Baseline Budgeting

States tend to use one of two different “baselines” when they consider a new budget. On the one hand, they may take the dollars spent in the previous year as the baseline. On the other hand, they may take the level of services that those dollars bought as the baseline. If they take the second approach, then price increases in services are automatically incorporated into the budgetary baseline. A study by economists Mark Crain and Nicole Crain suggests that spending grows about half a percentage point slower in those states that use dollars spent rather than services rendered as the baseline.<sup>33</sup>

<sup>25</sup> Daniel C. Vock, “Govs Enjoy Quirky Veto Power,” *Stateline*, Pew Center on the States, April 24, 2007, <http://www.stateline.org/live/details/story?contentId=201710>.

<sup>26</sup> For the law, see *Line Item Veto Act of 1996*, Public Law 104-130, 104<sup>th</sup> Cong. (April 9, 1996). For the Supreme Court decision, see *Clinton v. City of New York*, 524 U.S. 417 (1998).

<sup>27</sup> A bipartisan group of over 40 Senators has introduced such a bill. *Reduce Unnecessary Spending Act of 2011*, S. 102, 112<sup>th</sup> Cong., 1<sup>st</sup> sess. (January 25, 2011).

<sup>28</sup> Abrams and Dougan.

<sup>29</sup> Holtz-Eakin was the first to study the line-item veto in such a context. Douglas Holtz-Eakin, “The Line Item Veto and Public Sector budgets: Evidence from the States,” *Journal of Public Economics*, Vol. 36 (1988): 269-92.

<sup>30</sup> Besley and Case, “Political Institutions and Policy Choices: Evidence from the United States.”

<sup>31</sup> Vock.

<sup>32</sup> Crain, *Volatile States: Institutions, Policy and the Performance of American State Economies*, 111.

<sup>33</sup> Mark Crain and Nicole Crain, “Fiscal Consequences of Budget Baselines,” *Journal of Public Economics*, Vol. 67 (1998): 421-36.

### 8. *No Automatic Shutdown Provision*

In twenty-two states, the government automatically shuts down if, by the beginning of the fiscal year, policy makers have not reached an agreement on the budget.<sup>34</sup> A similar rule applies to the federal budget.<sup>35</sup> David Primo explains the theoretical effect of an automatic shutdown provision:

The legislature has the bargaining advantage because the governor, when considering a spending proposal, compares it to the outcome that would be obtained if he vetoed the spending proposal.<sup>36</sup>

Under these circumstances, “the legislature will be able to achieve its ideal budget, so long as the governor prefers it to no spending.”<sup>37</sup> In other words, the threat of a shutdown essentially permits the legislature to make a take-it-or-leave-it offer and that is enough to make the governor concede to their spending demands.

Empirical analysis seems to corroborate this theory. According to Primo, states without an automatic shutdown provision spend about \$80 less per capita.<sup>38</sup>

### 9. *Separate Spending and Taxing Committees*

Some states allow one legislative committee to have jurisdiction over both spending and taxing legislation. Others divide the two powers between separate committees. Intuitively, those states that keep these functions separate seem likely to spend less than those that combine them. The idea is essentially Madisonian: if one committee has jurisdiction over taxing but not spending then its members—unable to steer spending projects towards their constitutions—will have an incentive to block the interests of other committees with spending authority.<sup>39</sup>

The last researchers to publish on this matter were Mark Crain and Timothy Muris.<sup>40</sup> According to their data (which is from the 1980s), five states combine spending and taxing authority in one committee while the rest keep these two functions separate. They find that states with combined spending and revenue authority tend to spend \$1,241 more per capita than states with separate authorities. As indicated by Figure 1, this is by far the largest per capita effect of the institutions this paper surveys.

### 10. *Centralized Spending Committees*

Researchers have also examined the effect of centralizing spending authority in one committee rather than dividing it among several separate spending committees. In this case, the theoretical prediction is

<sup>34</sup> National Conference of State Legislatures, *Table 6-4: Procedures When the Appropriations Act is Not Passed by the Beginning of the Fiscal Year*, September 2008, <http://www.ncsl.org/default.aspx?tabid=12616>.

<sup>35</sup> At the federal level, shutdowns can also occur for other reasons. For example, the near-shutdown in August of 2011 was the result of the nation’s statutory debt ceiling.

<sup>36</sup> Primo, 102.

<sup>37</sup> Ibid.

<sup>38</sup> Ibid., 203.

<sup>39</sup> As the principal framer of the Constitution and as its chief advocate through the *Federalist*, James Madison advocated for checks and balances so that “ambition must be made to counteract ambition.” James Madison, “No. 51,” *The Federalist*, by Alexander Hamilton, James Madison, and John Jay, Clinton Rossiter, ed. (New York: Signet, [1788] 1961): 322.

<sup>40</sup> Mark Crain and Timothy Muris, “Legislative Organization of Fiscal Policy,” *Journal of Law and Economics*, Vol. 38, No. 2 (Oct., 1995): 311-33.

different: when a number of different committees have a hand in determining spending priorities, spending is subject to a “tragedy of the commons.” As Crain and Muris put it:

[N]o one committee has the incentive to restrain its spending commitments because the total level of spending is no longer the responsibility of any one committee. To the contrary, the resulting competition among committees to spend results in more spending than would otherwise occur, increasing reliance on deficit financing.<sup>41</sup>

John Cogan of the Hoover Institution and Stanford University examines this question at the federal level and finds that during periods in which the U.S. Congress had decentralized spending authority, spending grew much faster than in other periods.<sup>42</sup>

At the state level, Crain and Muris find that in the 1980s, 24 states had centralized spending authority in one committee, while the rest had spread it out among several committees. Their results corroborate the federal study by Cogan. They find that, on a per capita basis, states with centralized spending authority spend about \$199 less than those with decentralized spending authority.<sup>43</sup>

### 11. Annual Budgeting

Some state budget cycles last one year while others last two. Given the large number of complex projects that governments currently fund, biennial budgeting would seem to afford legislators the time to carefully scrutinize the budget in order to properly weigh the costs and benefits of different programs.

Indeed, Crain notes:

Since 1977 a number of proposals have been introduced in the U.S. House and Senate to lengthen the federal budget cycle from an annual to a biennial process. The perception behind these proposals is that a federal biennial budget would help curtail the growth of federal expenditures.<sup>44</sup>

But the theoretical relationship is not so clear. According to Paula Kearns of Michigan State University, a biennial budget might on the one hand shift the balance of power from the legislature to the governor. Since governors cannot export the costs of spending to other districts as legislators can, she reasons that this might lead to less spending. On the other hand, she notes that biennial budgeting introduces a measure of durability, which may make it more appealing for special interest groups to lobby for government largesse, thereby increasing spending.<sup>45</sup>

<sup>41</sup> Ibid., 314.

<sup>42</sup> Spending authority in the U.S. Congress was decentralized from 1886 to 1921 and then again from 1932 until the present. See John Cogan, “The Evolution of Congressional Budget Decision Making and the Emergence of Federal Deficits,” in *The Budget Puzzle: Understanding Federal Spending*, edited by John Cogan, Timothy Muris, and Allen Schick, (Palo Alto: Stanford University Press, 1994). See, also, David Brady and Mark Morgan, “Reforming the Structure of the House Appropriations Process: The Effects of the 1885 and 1919-1920 Reforms on Money Decisions,” in *Congress: Structure and Policy*, Matthew McCubbins and Terry Sullivan ed., (New York: Cambridge University Press, 1987).

<sup>43</sup> Crain and Muris.

<sup>44</sup> Crain, *Volatile States: Institutions, Policy and the Performance of American State Economies*, 102.

<sup>45</sup> Paula Kearns, “State Budget Periodicity: An Analysis of the Determinants and the Effect on State Spending,” *Journal of Policy Analysis and Management*, Vol. 13, No. 2 (1994): 331-62.

Kearns's empirical investigation supports the second hypothesis: a biennial budget cycle seems to increase spending.<sup>46</sup> Crain corroborates this result, finding that states with annual budgets tend to spend about \$119 less per capita than states with biennial budget cycles.<sup>47</sup>

### 12. *Small Senates*

A number of researchers have examined whether the size of a legislative chamber affects spending. The expectation has tended to be that larger chambers will spend more because each member has an incentive to spend in his or her own district while spreading the cost among all districts, and as the number of cost-sharing districts increases this incentive grows stronger.<sup>48</sup>

A number of researchers, using data at both the city and the national level, have found that larger unicameral legislatures do tend to spend more.<sup>49</sup> In bicameral legislatures, however, the more-seats-more-spending relationship holds in the upper house only. For example, Thomas Gilligan and John Matsusaka of the University of Southern California find that the number of state House seats has little or no effect on spending, but the number of Senate seats does. State Senates range from 21 to 67 members, and they find that a one-seat increase in membership is, on average, associated with about \$17 more in per capita spending.<sup>50</sup>

### 13. *Large House-to-Senate Ratios*

Why does the size of the House not affect spending? Jowie Chen, now of the University of Michigan, and Neil Malhot of Stanford University offer one reason. They observe that "lower chamber districts, at least in the United States, are unique because they are geographically embedded within Senate districts."<sup>51</sup> Thus:

[D]ividing each Senate district into more House districts has the effect of shrinking each House member's constituency, *ceteris paribus*. Having a smaller constituency dilutes House members' payoffs from exploiting common pool resources to fund large pork barrel projects.<sup>52</sup>

This means that adding more House seats should not have an affect per se, but increasing the ratio of House-to-Senate seats *should* lead to less spending. They corroborate this theoretical prediction with empirical analysis estimating that decreasing the Senate size by one seat can lower per capita spending by almost \$6, while increasing the House-to-Senate seat ratio by one unit decreases per capita spending by about \$45.

<sup>46</sup> Ibid.

<sup>47</sup> Crain, *Volatile States: Institutions, Policy and the Performance of American State Economies*, 112.

<sup>48</sup> The idea was formalized by Kenneth Shepsle and Barry Weingast, "Political Preferences for the Pork Barrel: A Generalization," *American Journal of Political Science*, Vol. 26 (February 1981): 96-111.

<sup>49</sup> See, for example, John Bradbury and Frank Stephenson, "Local Government Structure and Public Expenditures," *Public Choice*, Vol. 115 (April 2003): 185-98.

<sup>50</sup> Thomas Gilligan and John Matsusaka, "Deviations from Constituent Interests: The Role of Legislative Structure and Political parties in the States," *Economic Inquiry*, Vol. 33 (July 1995): 383-401.

<sup>51</sup> Jowie Chen and Neil Malhotra, "The Law of k/n: The Effect of Chamber Size on Government Spending in Bicameral Legislatures," *The American Political Science Review*, Vol. 101, No. 4 (Nov 2007): 657-76, 670.

<sup>52</sup> Ibid., 658. Emphasis original.

#### 14. "Citizen" Legislatures

In some states, legislating is a full-time job. Legislators work year-round, have large professional staffs, and are paid salaries that make outside work unnecessary. In other states, however, the legislative session is short, staffs are small, and legislators are paid too little to make legislating their only means of employment. The theoretical impact of a "professional" versus "citizen" legislature is unclear. A citizen legislator who spends most of his time outside of the capitol building might be more susceptible to the persuasions of interest groups than a professional who gets his information from paid staffers. On the other hand, citizen legislators, because they have other jobs, might not need the legislative job security that comes with appeasing interest groups.<sup>53</sup>

Economists Stephanie Owings-Edwards and Rainald Borck examine this question with an "index of professionalization" which includes factors such as legislative compensation, staff expenditure, and the length of legislative sessions. They find that a one-standard-deviation increase in professionalization increases spending by about 10.2 percent.<sup>54</sup>

#### 15. Direct Democracy

In the late 19<sup>th</sup> century, a number of states began experimenting with direct democracy by permitting their citizens to directly vote on legislation in statewide ballots.<sup>55</sup> Today, 27 states permit this sort of direct democracy in one form or another.<sup>56</sup>

Early studies of direct democracy at the state level concluded that it either had little effect on spending or that it boosted spending.<sup>57</sup> More recent studies that use larger data sets tend to find the opposite effect. For example, Matsusaka finds that an initiative with a 5-percent signature threshold (the most common threshold) is associated with per capita spending that is \$136 lower.<sup>58</sup> The economists Dale Bails and Margie Tieslau arrive at a similar result, concluding that the initiative tends to decrease per capita spending by about \$158.<sup>59</sup>

More recently, however, Besley and Case, ran a series of regressions and found that in most of them, the initiative had little impact on spending.<sup>60</sup> Matsusaka has suggested one way to reconcile all of these findings. He argues that the effect of direct democracy switched at some point in the last several decades,

<sup>53</sup> There are a number of other reasons on each side of the argument.

<sup>54</sup> Stephanie Owings and Rainald Borck, "Legislative Professionalism and Government Spending: Do Citizen Legislators Really Spend Less?" *Public Finance Review*, Vol. 28, (2000): 210-25.

<sup>55</sup> An issue placed on the ballot by petition is an initiative. When the legislature places it on the ballot, it is a referendum. For an overview, see John Matsusaka, *For the Many or the Few: The Initiative, Public Policy, and American Democracy*, (Chicago: University of Chicago Press, 2008).

<sup>56</sup> For this and other data on direct democracy, see *The Initiative and Referendum Institute*, The University of Southern California, <http://www.iandrinstitute.org/>.

<sup>57</sup> Jeffrey Zax found that initiatives were associated with higher levels of spending. See Jeffrey Zax, "Initiatives and Government Expenditures," *Public Choice*, Vol. 63, No. 3 (1989): 267-77. Paul Farnham found no impact. See Paul Farnham, "The Impact of Citizen Influence on Local Government Expenditure," *Public Choice*, Vol. 64, No. 3 (1990): 201-12.

<sup>58</sup> John Matsusaka, "Fiscal Effects of Voter Initiative: Evidence from the Last 30 Years," *Journal of Political Economy*, Vol. 103, No. 3 (1995): 587-623.

<sup>59</sup> Dale Bails and Margie Tieslau, "The Impact of Fiscal Constitutions on State and Local Expenditures," *Cato Journal*, Vol. 20, No. 2 (Fall 2000): 255-77.

<sup>60</sup> In one specification, it did seem to be associated with lower levels of income taxation per capita. Besley and Case, "Political Institutions and Policy Choices: Evidence from the United States."



and that direct democracy was associated with more spending in the early part of the 20<sup>th</sup> century and less spending in recent decades.<sup>61</sup> This may be the result of changing public attitudes toward spending.

### 16. Term Limits

Does limiting the time a politician can spend in office affect spending? Some proponents of term limits have argued that they break-up the political culture of spending.<sup>62</sup> But not everyone agrees. Some researchers make the case that term limits remove an important check on politicians by freeing them from the necessity of seeking voter approval in their final terms.<sup>63</sup>

The empirical investigations of term limits have not clarified matters. Consistent with the view that term limits lead to more spending, Besley and Case find that Democratic governors tend to spend more in their second terms when they cannot run again.<sup>64</sup> Using a larger dataset, they recently reexamined the question and observe an odd pattern. Like direct democracy, the effect of gubernatorial term limits seems to have changed over time. They conclude that gubernatorial term limits lead to more spending in the 1950s, 1960s, and early 1970s, but seem to be associated with less spending from the mid-1970s onward.<sup>65</sup> Unfortunately, they write, “We can offer no simple explanation for this pattern.”<sup>66</sup>

The effects of *legislative* term limits are no clearer. In their 2000 study, Bails and Tieslau find that legislative term limits reduce per capita spending by about \$173.<sup>67</sup> But a more recent study by the political scientist, Abbie Erler, finds that states with more restrictive legislative term limits actually spend about \$212 more per capita than others.<sup>68</sup> In sum, it seems that the evidence on term limits is decidedly mixed.

### Conclusion

Absent policy change, governments at all levels—and those who have come to depend upon them—face a bleak future. According to projections, both federal and state spending growth is unsustainable, threatening to push debt-to-GDP ratios well past 90 percent in a matter of decades.<sup>69</sup> The 90-percent mark is important because that is when research suggests that debt begins to hamper economic growth.<sup>70</sup>

<sup>61</sup> John Matsusaka, “Initiative and Referendum” in *Encyclopedia of Public Choice*, Charles Rowley and Friedrich Schneider, ed. (USA: Springer, 2004).

<sup>62</sup> On the culture of spending, see James Payne, *The Culture of Spending: Why Congress Lives Beyond Our Means*, (USA: ICS Press, 1991).

<sup>63</sup> Timothy Besley and Anne Case, “Does Political Accountability Affect Economic Policy Choices? Evidence from Gubernatorial Term Limits,” *Quarterly Journal of Economics*, Vol. 110, No. 3 (1995): 769-98.

<sup>64</sup> *Ibid.*

<sup>65</sup> Besley and Case, “Political Institutions and Policy Choices: Evidence from the United States.”

<sup>66</sup> *Ibid.*, 55.

<sup>67</sup> Bails and Tieslau.

<sup>68</sup> Abbie Erler, “Legislative Term Limits and State Spending,” *Public Choice*, Vol. 133 (2007): 479-94.

<sup>69</sup> According to the CBO’s alternative fiscal scenario (which assumes no change in *policy*), federal debt held by the public will exceed 90 percent of GDP within a decade. See Congressional Budget Office, *op. cit.* And according to Miron, 17 states will have accumulated net debt levels in excess of 90 percent of GDP by 2030. See Miron, *op. cit.*

<sup>70</sup> Carmen Reinhart and Kenneth Rogoff, “Growth in a Time of Debt,” (working paper, National Bureau of Economic Research, 2010), <http://www.nber.org/papers/w15639>.

A handful of policies seem to be driving the problem: Medicaid, pensions, and other post-employee benefits loom large.<sup>71</sup> But these policies—like all policies—are themselves the products of the institutions that helped create them, the rules that influence political outcomes at the state level. These institutions and their impact on spending have been the subject of extensive study. This paper reviews this research and highlight more than a dozen institutions that have been shown to limit spending, limit the growth of spending, or limit the volatility of spending.

After converting all per capita estimates into 2008 dollars, it is clear that separate taxing and spending committees and item reduction vetoes have the largest effect on per capita spending. These institutions also happen to be among the least-studied and so further analysis may be warranted. Among the most-studied of institutions are strict balanced budget requirements, supermajority requirements for tax increases, and tax and expenditure limits.

In many cases, subsequent study of institutions has yielded more nuanced results. For example, a number of the institutions this paper discusses are only effective in certain circumstances or when they are designed in a certain way. This suggests that we may still have much to learn about the institutions that have received comparatively less attention, such as item-reduction vetoes. Nevertheless, policy makers interested in arresting the unsustainable growth of government seem to have a number of tools at their disposal.

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<sup>71</sup> State and Local Governments: Fiscal Pressures could Have Implications for Future Delivery of Intergovernmental Programs, *Government Accountability Office*, No. 10-899 (July 2010), <http://www.gao.gov/new.items/d10899.pdf>.

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Chairman ENZI. Thank you.  
Dr. Meyers.

**STATEMENT OF ROY T. MEYERS, PH.D., PROFESSOR OF POLITICAL SCIENCE AND AFFILIATED PROFESSOR OF PUBLIC POLICY, UNIVERSITY OF MARYLAND, BALTIMORE COUNTY**

Mr. MEYERS. Thank you, Chairman Enzi and the Committee, for the invitation to testify and particularly for holding this hearing. It is a very important topic. I am just going to summarize my written testimony, but I want to start by agreeing completely with the main point in your opening statement, that we need to think about how the budget process can help us design, fund, and oversee the programs so that they will improve the lives of American citizens.

So how well is the budget process currently structured to do that is the next question, and there are actually some good, positive attributes to the current process. We have the executive budget. We have used GPRA to increase the level of performance management in the executive branch. You are able to draw on the expertise of staff, including CBO and GAO. And, in addition, you are legislators. You go back home, and you listen to your constituents, and you can use those experiences to try and understand what their goals are and how they evaluate the programs themselves.

But there is one main barrier to using the process to allocate resources to the programs that you want to fund, and that is the features of the Congressional Budget Act, in particular the segmentation of discretionary and mandatory and tax spending from each other. So most of my testimony focuses on that.

You deal with those situations when you try to enforce the budget process. Last year, for example, you rightly tried to control phony savings from CHIMPs. But, on the other hand, when you think about it carefully, you want to be able to have a competition between discretionary and mandatory spending, and between those types of spending and tax spending. So this is why I think the portfolio approach proposed by Redburn and Posner should be adopted, and you should experiment with it very seriously over the next couple years.

But I think that is actually only part of the puzzle, that you also have to look at how the Congress is structured to be able to utilize those performance reviews if they give you good information about which programs should be continued and which should be stopped.

Imagine, for example, if you received a portfolio review about the foreign aid programs or the housing programs that you put on display at the beginning of this session. How would you deal with those performance reviews? Could you use a budget resolution to tell the committees to rationalize those programs? And I think the clear answer is no, the budget resolution process is too weak to be employed to force those savings. And for that matter, it should not be just about savings. It should be about trying to find programs that work so that American citizens' lives will improve.

So then the question is: What could be done to improve this process? And I think you are going to have to consider non-incremental reforms to really make a big difference. I think biennial budgeting is actually a very interesting topic and is worth considering seri-

ously, but I think it is going to have relatively little effect unless you make some other changes.

So I am going to propose two non-incremental reforms. First of all, though, I want to acknowledge that the problems that we have with the budget process are not simply because of the flaws in the budget process itself. When you are budgeting, you are making very difficult decisions, and you have very big differences on policy between the parties, and actually sometimes within the party. When there is very little trust between the parties, that is a big problem.

So, that is something you just have to acknowledge, but you also need to use the budget process to allow you to express those differences. This is a democratic system, and you need to be able to reflect your constituents' different wishes.

You can go overboard on that, however. In other words, you can continually express their wishes in opposition to each other and then not pass bills on time and not eliminate wasteful spending and move the money towards more useful spending.

So what in particular I think you should do is, first of all, have a serious conversation about how the Committee structure in Congress could be revised. And, in particular, that would mean collapsing the appropriations and authorizations process so that there would be a committee with expertise on each sector of the budget—each sector of Government policymaking. In other words, you would eliminate the Appropriations Committee, but everybody would be an appropriator. All the authorizing committees would be appropriating in their area of expertise for discretionary and mandatory spending and also jointly with the Finance Committee on taxes.

Think about the budget problems that we face now. If you look into the medium term, it is the health budget that is the most scary, right? There is excess cost growth. That is continuing. And we also have very low quality health outcomes in this country compared to how much we spend.

We could have a better way of dealing with that challenge of health spending if we had a Health Committee, a committee that had jurisdiction over discretionary and mandatory spending and tax expenditures.

Now, of course, there are massive political difficulties in moving to that approach, but on occasion, Senators are brave enough to propose it. The last time it was considered really seriously was in 1993 when Senator Kassebaum, a moderate Republican, put together a proposal, and I think you should return to that bill, look at it again, and consider it seriously. In fact, if you do, I think you would realize that it has some potential to deal with some of the problems you have described in previous hearings, such as expired authorizations and regulatory issues, because, for example, that Health Committee would have jurisdiction over regulatory policy for health, and it could figure out how those regulations relate to mandatory and discretionary spending and tax preferences.

One other point that Senator Kassebaum made back in 1993 was to rename your Committee the "Committee on National Priorities." I think you should take that title and you should take that as your mission. And when you think about it, sometimes in budgeting we

focus far too much on costs without thinking about the outcomes of costs or why we are actually spending money.

In the case of the portfolio approach that Posner and Redburn proposed, they realized that the executive branch is far ahead of the legislative branch in doing this kind of work, they would give a push to the executive branch's ability to rationalize programs. But your job is also to create value for American citizens by accurately assessing conditions in the country and the world and by setting goals for programs that would seek to improve them.

So I want to give you one example that I think illustrates the limitations of what we do now in both the executive branch and the legislative branch, and I am glad that Senator Whitehouse is here because it relates to climate change.

The Obama administration, if you look at the priority goals for climate change, is focused on reducing the Federal Government's greenhouse emissions.

We all know that the Obama administration has a much more aggressive goal for the whole country to deal with climate disruption. Personally, I think that is a great idea, and I really appreciate Senator Whitehouse's eloquent and persistent advocacy on this issue.

But whatever you think about climate disruption, that should be a big issue that you should be considering when you are writing a budget. You should not be wasting your time fighting over CHIMPs and lots of points of order on the budget. You are the corporate board of America in some sense. You are supposed to be setting policy and overseeing how the executive branch carries it out, instead of, for example, debating on the vote-a-rama or creating a very long list of reserve funds that we all know are symbolic.

So if you want to live up to your image as the world's greatest deliberative body, I think you need a better way of identifying the goals you have for the country. And I want to give you one example of how you could do that.

I would suggest that you ask the executive branch to compile an annual report that you would call "The State of the Nation." It would take data about what conditions are like in this country, and then with that report, you could evaluate the claims and promises made in the State of the Union speech.

In fact, some States already do something like this. I am glad Senator Kaine is here. Virginia Performs, I would encourage you to look at that website. It is an excellent website that describes the nature of life in Virginia, where things are getting better, where things are getting worse, and it provides useful input to their own budget process.

After that report would be released, I think you should have a debate about it. Right now you get views and estimates reports from the different committees. You can find them on the Internet, but it is not very clear that they are used well. So I think instead it would be useful to have a couple weeks of debate prior to the consideration of the budget resolution which would be about the true state of the Nation.

And, of course, that debate would highlight your partisan disagreements. Good. But it also might highlight some agreements that are the potential base for a budget resolution.



For example, President Obama proposed this year a big increase in funding for cybersecurity. I have not heard anybody say that is a bad idea—or maybe I should rephrase that. I have not heard anybody say that we do not have to worry about cybersecurity. That should be the kind of debate that you have before a budget resolution, and then you can think about what policy tools, using discretionary and mandatory spending, and tax spending, could help address the goal of improving cybersecurity problems.

So I want to conclude by saying that at this stage of the budget process, setting priorities across sections of the budget is always going to be your most difficult task. You are on the Committee that has the hardest job. There is no question about it. And in part because there is not a convenient metric for comparing guns and butter, you have to rely on politics to resolve some of those differences, and I think that is a good idea. Voting is a good idea. Lobbying is a good idea. Elections are great. Partisanship, ideology, they are all necessary to help set the course of the country. But what we have now is a bad politics. We are not—let me rephrase that. We do not have a structure in Congress to allow you to make the politics as helpful as possible to make allocations across the budget.

So thank you for giving me the opportunity to testify, and I would be glad to answer any questions.

[The prepared statement of Mr. Meyers follows:]

Testimony before the U.S. Senate Budget Committee  
April 13, 2016

on  
Fixing the Broken Budget Process: Outcome Budgeting to Maximize Citizen Value

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Chairman Enzi, Senator Whitehouse, and Members of the Committee, thank you for inviting me to testify on this important topic. Thank you also for holding this series of hearings, for budget process reform is greatly needed.

Most flaws of the current process are well known. Congress often does not enact budget resolutions, and regular appropriations bills are enacted far too late, if at all. Confidence is justifiably low that budgeting supports wise counter-cyclical management of the economy and avoidance of financial problems over the long-run. And the process is too complex. Your constituents don't understand how budgeting is supposed to work, and it's no wonder that they don't.

Some of that complexity is the result of well-intentioned previous reforms. By adopting and amending the Congressional Budget Act, Congress created rules designed to develop and enforce budget limits. Yet consider the situation in which you now find yourself. The Budget Control Act's discretionary caps, as set after the "Supercommittee" did not reach agreement,

were then adjusted for short terms in both 2013 and 2015. Few participants believe that the caps scheduled for the remaining years will hold, given their potential effects on spending for infrastructure, research, education, the disadvantaged, and national security.

If this is correct, and if baseline projections are accurate about growth in mandatory spending, especially for net interest, medium-term fiscal risks are worrisome. Concern about those risks might lead Congress to again search for so-called “action-forcing” process reforms. But the experiences under both Gramm-Rudman-Hollings and the Budget Control Act show that it is extraordinarily difficult to force deficit reductions, particularly for mandatory spending and for tax expenditures (which below I call “tax spending”).<sup>1</sup>

This is why the topic for today’s hearing is so timely. As important as it is to limit the debt exposure of the federal government, this is not the only goal Congress should hold for the budget process. Congress should also want to use the budget process as one of its main tools for designing, funding, and overseeing public policies that will improve the lives of American citizens. If the process is used to eliminate low priority spending, that will help prevent unnecessary debt. Adding effective spending for high priorities can grow the economy and address many important goals citizens hold for their nation and the world.

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<sup>1</sup> Roy T. Meyers, The Implosion of the Federal Budget Process: Triggers, Commissions, Cliffs, Sequesters, Debt Ceilings, and Shutdown, *Public Budgeting and Finance*, 34:4, Winter 2014; <http://userpages.umbc.edu/%7Emeyers/implosion.pdf>.

It is therefore important to ask: Which features of the current budget process enable you to make allocations to the most efficient and effective programs that address high priority goals? And which features have the opposite effect, serving as barriers to generating value for citizens?

The situation is not entirely bleak, for we can answer the first question by identifying some positive attributes that lead to good allocations. The decision in 1921 by Congress to delegate budget preparation to the President has led to a sophisticated budget preparation system that rules out many bad allocations and generates some good ones. The laws you passed in 1993 and 2010, the Government Performance and Results Act (GPRA), and its Modernization Act (GPRAMA), stimulated significant performance management advances in the executive branch. You draw on the valuable expertise of the Congressional Budget Office (CBO), the Governmental Accountability Office (GAO), and committee staff. And as legislators who regularly interact with your constituents, you stay informed of their values and experiences--helping you determine what goals to emphasize and what programs to fund.

On the other hand, there are many features of the current process that make it extraordinarily difficult for you to make the allocations that will best serve the American people. An especially notable barrier is how responsibility over most sectors of the budget is fragmented between discretionary, mandatory, and tax spending. This is due to the original design of the Congressional Budget Act, which overlaid a new process on top of traditional committee jurisdictions. The fragmentation of the process was then enhanced by the enforcement procedures of the 1990 Budget Enforcement Act and the 2011 Budget Control Act.

As your committee knows, those enforcement procedures are imperfect. Last year you worked to prevent phony savings from “CHIMPs,” changes in mandatory spending claimed in appropriations bills. It is desirable to stop gimmickry. Yet the traditional segmentation of discretionary and mandatory spending makes it extraordinarily difficult to make intelligent tradeoffs across these categories for many sectors of the budget. Why does this defect continue? It is hard to think of a policy justification, leaving the plausible political explanation that it has been maintained only to protect turf.

To improve its ability to make budget allocations, Congress will need to address this fundamental flaw in the budget process. This is why you should support the “portfolio budgeting” approach suggested by Redburn and Posner.<sup>2</sup> In their paper for the National Budgeting Roundtable, they provide two examples of the many sectors of the budget where the government’s efforts are divided between discretionary, mandatory, and tax spending: higher education and housing. These different types of spending should be compared to each other when making budget allocations for these sectors. Yet in the executive branch, the budget process focuses on spending by departments, and is insufficiently coordinated with review of related tax expenditures. For example, the informative Program Assessment Rating Tool, or PART, developed by the George W. Bush administration, applied only to departmental spending;

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<sup>2</sup> F. Stevens Redburn and Paul L. Posner, Budgeting for National Goals, Working Paper #2, National Budgeting Roundtable, George Mason University, August 2015; <http://psc.gmu.edu/wp-content/uploads/New-Ideas-for-Federal-Budget-Working-Paper-No.-2.pdf>.

it did not cover tax expenditures. Ignoring education and housing tax spending meant that the PART was aptly named.

Redburn and Posner recommend the better approach of viewing all government efforts in a budget sector as a “portfolio.” This is an excellent metaphor for what budgeting should do. As with well-designed investment portfolios, it recognizes the desirability of diversity. In the case of policy, this means government applying different policy tools to typically variant conditions across the country. The budget portfolio metaphor also reminds us of what a smart job seeker will do when constructing a portfolio of past achievements and current skills that can be shown to potential employers. That job seeker will highlight positive accomplishments, weeding out attempts that didn’t fully succeed or that are no longer relevant, and suggest how future accomplishments are likely. This is similar to how budgeting should work--selecting from current activities to determine which deserve continuation, and concentrating resources on promising new alternatives.

The portfolio approach recommended by Redburn and Posner would build on executive branch achievements in strategic planning and in measuring and managing performance. They are correct in noting, though, that “the current GPRAMA process lacks explicit connection to the budget process;” it instead emphasizes quarterly reviews for those managing to the President’s priority goals.<sup>3</sup>

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<sup>3</sup> Ibid, p 16.

The President's priority goals are affected by the statutes you pass and the budgetary resources you provide. But in general, the executive-legislative branch consultations mandated by GPRAMA and its predecessor have not been influential. While Congress has required the executive to engage in various "outcome budgeting" activities, it has not demonstrated a similar commitment to using the information generated by these activities.

One cause of this problem is the way Congress is organized. Imagine that the executive branch did present Congress with a detailed portfolio review for higher education or for housing, or if Senate Budget Committee staff prepared a similar analysis with assistance from CBO and elsewhere. Imagine also that this review proposed a reallocation of funds within the portfolio that would rebalance the discretionary, mandatory, and tax spending categories. What would happen next? Would the current budget process help Congress consider and then act on the recommendations of the portfolio review?

It would not. The budget resolution process is too weak to direct reallocations across the fragmented committee structure. At best, Congress could experiment with ad hoc procedures to cross committee and enforcement boundaries, but this is something that Congress has tried only in rare circumstances, as it did with the Carter energy plan. So you should be asking: What reforms might better enable Congress to utilize portfolio reviews? More generally, how can Congress help improve government's ability to make budget allocations both within and between sectors of the budget?

In the remainder of this testimony, I will propose that you consider two non-incremental reforms. But first, I need to acknowledge that budgeting is difficult not simply due to the flawed design of the process. Its problems result just as much from the big differences on policy between the parties, and the political risks of attempting to resolve those differences. Reaching agreements on sensible compromises--typically required for our checks and balances system to work well--is now impeded by low levels of trust between the parties, and sometimes within them. This is true even for situations in which you might expect it would be easier to compromise, such as in a budget conference, where agreeing to a number between two proposed amounts is a traditional practice.

This means that reforms to the budget process must accommodate--even celebrate--your desire to express your differences over policy issues. At the same time, those reforms should enable you to waste less time and to adopt workable policies. When you consider how proposed reforms might simultaneously help you meet these different goals, it is important to keep in mind that Congress, like any institution, learns as it goes. This means that you should be cautious about immediately dismissing a proposed reform because it would require some difficult adjustments from current practice. This inevitable cost should be balanced against the possibility that a reform will produce significant benefits after several years of implementation.

In my opinion, the alternative with the greatest potential for improvement is a comprehensive reorganization of the committee structure and a simplification of related procedures. This is an extraordinarily complex topic, so today I will not discuss all of its



important components. Its basic virtue would be a better alignment of committee authority and expertise with the various sectors of government activity. This would allow each responsible committee to make strategic policy decisions and budget allocations within its sector. For example, there would be a Health Committee, with jurisdiction over all discretionary, mandatory, and tax spending, as well as regulatory policy, for the health sector. Given the long-term challenges presented by excessive spending on health, and the need to improve health outcomes for many Americans, it should not be hard to see the advantage this structure would have over the currently fragmented system and process.

For most people in Washington, at most times, committee reorganization and process simplification is a great unmentionable, for obvious political reasons. Yet experts on budgeting and policy-making have periodically made persuasive cases for reorganization. In 1986, following her founding directorship of the Congressional Budget Office, Alice Rivlin gave her presidential address to the American Economic Association, calling for streamlining the Congressional budget process.<sup>4</sup> In 1993, Senator Kassenbaum proposed a well-designed restructuring of committees by sector, giving them both authorizing and appropriating responsibilities.<sup>5</sup> The bill would also have renamed your committee as the Committee on National Priorities, which is a good description of what you should aspire to set.

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<sup>4</sup> Alice M. Rivlin, "Economics and the Political Process," *American Economic Review*, 77: March 1987, pp. 1-10.

<sup>5</sup> <https://www.congress.gov/bills/103rd-congress/senate-resolution/13/text>.

In previous hearings in this series, your committee has investigated biennial budgeting, unauthorized spending, and regulatory budgeting. Reorganization and simplification would make it much more likely that Congress could periodically undertake concentrated reviews of budget sectors using a rolling reauthorization schedule. Congress could require the administration to support this schedule by mandating production of Quadrennial Reviews for all sectors of the budget; DoD and several other agencies already prepare such reviews.

Reorganization and simplification would also reduce unproductive redundancy, such as the need to pass two very similar bills each year for national defense. Regarding regulatory policy, incorporating a retrospective review of existing regulations into a strategic review of spending programs has a better potential for aligning the incentives created by the federal government. It would not replicate the worst parts of the budget process, as I fear would be the case under a regulatory budgeting process.<sup>6</sup>

The political benefits from reorganization and simplification could also outweigh the costs of transition to this modernized approach. If all sectoral committees have control over spending in their unified jurisdiction, and all legislators are members of several committees, each legislator will be guaranteed influence over a significant part of the budget, subject to the constraints set by the budget committees. Procedures could also be developed to allow a limited number of amendments on each bill, meaning that proponents and opponents of programs would

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<sup>6</sup> Roy T. Meyers, "Regulatory Budgeting: A Bad Idea Whose Time Has Come?," *Policy Sciences*, 31: December 1998, pp. 371-384; <http://umbc.edu/%7Emeyers/regbud.pdf>.

have the opportunity to engage in a fair fight over how funds would be allocated across all programs in a sector of the budget.

The second major approach to reform that I think you should seriously consider relates to Senator Kassenbaum's idea of renaming your committee as one that would address national priorities, rather than “just” the budget. The emphasis in budgeting has always been on controlling government costs, which are easier to measure than outcomes and which must be financed. But you can’t budget well without thinking about why you are spending money; thus the call for “outcome budgeting,” of which there are many variants.

The current administration’s emphasis under GPRAMA has been managerial accountability for reaching its priority goals. This is an appropriate focus for the branch that is tasked with the faithful execution of laws. It is also something to which Congress should pay attention through its oversight activities. But carrying out existing laws is only part of your responsibility and of the President’s. Creating value through your policy-making also requires accurate assessment of the conditions in the country and the world, and setting goals for programs that seek to improve those conditions.

As a country that has a very advanced form of government in many respects, the United States already does a great deal of condition assessment and goal-setting at the program level. The accuracy and transparency of government data is often outstanding. And it is a rare agency that hasn’t been given numerous, often difficult goals that it should seek to attain.

Nevertheless, there are limitations to the current approach. Consider the Obama administration's priority goals on "Climate Change (Federal Actions)." The goal statement is to:

More than double Federal government consumption of electricity from renewable sources to 20% by 2020 and improve energy efficiency at Federal facilities as part of the wider strategy to reduce the Federal Government's direct greenhouse gas emissions by 40 percent by 2025.<sup>7</sup>

Note that the goal is only for the federal government. Of course, the administration has a much more ambitious goal for reducing climate disruption that applies to all of America rather than to just the federal government, as shown by its support of the Paris Agreement. My own preference is that this national goal be made even stronger, and communicated more widely by the administration, and for that reason I want to thank Senator Whitehouse for his persistent and eloquent advocacy of this position.

Whatever your position on climate disruption, the general point here is that such big issues should be your emphasis, rather than arcane disputes over CHIMPs and the like. In the current process you do get around to some of those big issues, but often indirectly, such as when you consider how national security or the country's infrastructure will be hurt by an arbitrary ceiling on all discretionary spending.

What is missing, therefore, is a national strategy, or more accurately, a deliberation that would point towards one. I am not proposing that in setting national priorities you should do anything that would resemble the top-down planning sometimes used by authoritarian

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<sup>7</sup> <https://www.performance.gov/node/3406/view?view=public#overview>.

governments--far from it. Instead, I would like the Senate to have the opportunity to live up to its self-image as a world-class deliberative body. This would be more likely if it modified how it constructed its budget resolution, or alternatively, developed a national priority statement that would accompany its annual or biennial budget resolution. That is, if you are going to shift towards outcome budgeting, you need to be clearer about what outcomes you want the budget to emphasize. To what extent will the U.S. attempt to mitigate and adapt to climate disruption? To promote its exports abroad? To eliminate child poverty? To control migration? And so on.

Consider how the process works now. Each year you assemble to hear the President's State of the Union speech, and you receive the President's budget. The speech and the budget make many claims and propose numerous initiatives, and are followed by your mixed reactions, organized generally along partisan lines. In years in which you find it possible to pass budget resolutions, sometimes those resolutions are accompanied by comprehensive but not always realistic plans for modifying budgets and policies. In other years, the resolutions only set out budget aggregates, functional allocations that are not binding, and numerous "reserve funds" that are mostly symbolic.

There may be feasible alternatives that would allow you to better express your views about the nation's priorities and to incorporate some of these findings into the budget resolution. One would be to require that the executive branch compile data on its priority goals, and on similar goals stipulated by vote of Congress, into an annual report that would be published around the time of the President's budget submission. It could be called *The State of the Nation*,

to which claims made in the State of the Union speech could be compared. Several states now present such information to their citizens through easy-to-use web sites, such as [Virginia Performs](http://vaperforms.virginia.gov/).<sup>8</sup>

Following the release of *The State of the Nation*, and the President's budget, the Congress could designate several weeks during which the parties could debate on how well America is doing and how it might improve. This would be a modernization of what are now the committees' "Views and Estimates" reports to you. Your committee could then write a budget resolution, having been informed by the debate. That debate will undoubtedly highlight disagreements, but it will likely also reveal agreements, on which the start of a successful resolution might be built. This will be particularly the case should you seriously consider shifting from a concurrent budget resolution to a joint budget resolution, which is a desirable reform in my opinion, but also a topic for another time.

To be clear, this stage of the budget process--setting priorities across sectors of the budget--will always be the most difficult. There isn't a convenient metric for weighing the relative values of "guns vs. butter," or many of the other difficult cross-sectoral choices you must make. Politics--partisanship, ideology, lobbying, and votes--will unavoidably and justifiably be central to the process. What you should seek, though, are ways to make those politics produce better outcomes. This can be done by commissioning the generation of better information, by

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<sup>8</sup> <http://vaperforms.virginia.gov/>.

reorganizing the committee structure, by simplifying budgetary and legislative procedures, and by debating big issues.

I would be glad to answer questions you have. Thank you again for the opportunity to testify.

Chairman ENZI. Thank you, and, again, thank you for the written testimony that all of you have given. That will be a part of the record as well.

I am going to defer to Senator Whitehouse, and that way Senator Perdue can have an opportunity to speak before he has to leave for a different committee.

Senator WHITEHOUSE. Would he like to go now? I am perfectly happy to yield. Okay.

First of all, Dr. Meyers, thank you for the compliment. I appreciate it. I was just asked to resign—or apologize to the fossil fuel industry by a witness in another committee—you can hardly imagine which one, I am sure—today, so to have your kind words is sort of an offsetting principle. Somewhere in the middle I suppose is the truth.

Your point about cybersecurity I think is significant because one of the things that has frustrated the executive branch about dealing with Congress on cybersecurity has been the fact that the cybersecurity issue touches on—I think they used to say to me 38 committees and subcommittees. How do you possibly mollify 38 committees and subcommittees as you try to make change?

So if we are going to go into in some fashion the business of setting budget parameters based around issues, we may find that we have a better case to make against rival committees and jurisdictions if we confine ourselves to those issues where the substance of the issue is so spread across so many committees that it is very hard for anybody to claim that they really have guidance over it. I think that concern is one we will have to get into gradually.

The other point that Chairman Enzi has made is that where there are multiple programs, we might be a force for trying to bring a little bit of more common-sense regularity to them and streamline them. And I think in principle that makes sense, but as I said about the veterans, there are circumstances where doing things through different agencies actually makes considerable sense, and I think that is an example. So we would have to be watchful about that, and I would be interested in the comments of the witnesses on where they feel that—or by what standards would you judge what is a sensible differentiation versus just duplication and waste? And are we on the Budget Committee actually the ones best suited to do that?

The last thing I will say—and then I will give the witnesses a chance to respond to that point—is that I thought it was very important that the witnesses agreed that you have to look at our spending on a more unitary basis, that if you look only at budgeted spending and do not look at mandatory spending and do not look at tax spending, then you are dealing with only a very small subsection of the problem. And I would say for my purposes the tax spending is particularly overlooked, but also a particularly ripe area for oversight, because if you are a wily special interest, you do not go to Appropriations to fight for an appropriation every year. That is sucker's work. You go to the Tax Code, and you get your special interest exception baked in. And once it is in, it is there forever, and all you have to do is defend it. And so we now have more money going out the back door of the Government revenue house through tax spending than we do going out the front



door through regular cash spending. And we really need, I believe, to get our arms around that.

But in my remaining time, I would ask if any of the witnesses have any thoughts about that conundrum of how we pick apart on Chairman Enzi's screen which of the 40 programs should or should not be. Is that something we have hearings on? What are your thoughts on the limitations on just trying to unify all these Federal programs?

Mr. POSNER. I will take that first, I think there are a couple things.

One, ideally it would be good, assuming we do not reach the restructuring that Dr. Meyers talked about, for this to be a concerted initiative between the Budget Committees and the authorizers, recognizing that the Budget Committees bring something the authorizers do not. You see the whole picture. You technically have jurisdiction over tax expenditures, regulatory programs, discretionary and mandatory programs. I think that is an important thing to look at, whether you are looking at higher education, housing, community assistance, economic development assistance, any area that really cuts across so many committees. I mean, this is the one Committee that can at least lay claim to starting. The other thing I think—

Senator WHITEHOUSE. Let me cut you off there.

Mr. POSNER. Yes, go ahead. Sure.

Senator WHITEHOUSE. Because my time has expired. I am going to stay until the end, so we can continue this conversation once all the other Senators have had a chance to say their piece. But I do not want to cut unduly into Senator Perdue's time, so let me ask you to suspend, and I will yield, and we can follow the conversation later at the end of the hearing.

Senator PERDUE. Well, thank you for that courtesy. I will be brief.

Dr. Posner, you have given testimony before, and I could not agree with each of you more. And I want to commend our Ranking Member today, Senator Whitehouse. We are on different sides of several issues, but on this issue I think we are aligned. I think he has offered up some very thoughtful and productive recommendations, and I think this is a process that we have got to start.

Dr. Meyers, I agree 100 percent with you. We have got to go big at this point, given the size of the financial crisis and the irresponsibility we have seen up here over the last 20 years—among both parties. This is not a partisan problem. We both created it.

I have two questions, really. I would like to get you to speak more about Senator Kassebaum's idea back in 1993 about the combination of and the benefits of streamlining this process. One of the problems I think we have is that we have a budget resolution now that is not a law. It is a resolution. We pass it with 51. So the majority crams it down the throat of the minority. Then we go to an authorization process, which is at 60 votes in the Senate, and an appropriation that is at 60. So the minority party is always protected and can just do nothing and push us into a non-funding situation at the end of the year. This is structural. I understand that. But I know that in 1993 they talked about potentially combining

that among—focusing on the policy committees where most of the understanding of the day-to-day oversight of these departments.

The second piece of that is reorganizing that around the outcome that you want to achieve. Mr. McTigue, I know you have written about that as well. In your experience in New Zealand, you actually achieved that. So would you respond to that?

Then, also, the constraint around—the Article II constraint that we have, where the executive branch here is not a participant, basically, according to the Constitution. When you look at other performing governments, State governments, foreign governments, even corporations, you have got one commonality, and that is a strong executive participation in the budget and the spending process. We have a limitation constitutionally. Can you guys speak—I would love all three of you to speak to that quickly, if you can, in the time remaining. And thank you, Senator Whitehouse, for your courtesy.

Senator WHITEHOUSE. My pleasure.

Mr. MEYERS. So those are very important points, and we do not have time to discuss all the fine details of them. But regarding the lack of Presidential involvement, that is particularly true at the budget resolution stage, and periodically there has been serious consideration of the idea of a joint budget resolution, which, in my opinion, would not hurt Congress' Article I power of the purse but, rather, just realize that the President is an equal player. Obviously, he has the ability to veto appropriations bills and can set limits, just as you can. I would be glad to talk to you more about that later.

The point about Kassebaum's approach and of the general idea of committee restructuring is—there are two, actually, two advantages. One is you would be able to rely on the committees to make major decisions. Those committees would be representative of the floor from both parties, but they would be the experts. You actually have, of course, a great deal of expertise now in the committees, but sometimes they are organized in a way that is redundant, somewhat similar to the GAO studies that you cite repeatedly. I watched your expired authorizations hearing, and I remember Senator Ayotte saying, why are we passing a national defense authorization and a defense appropriations bill that are almost indistinguishable in their content. And since you seem to have a great difficulty coming up with floor time to address big issues, it seems a normal idea would be to say let us take a concerted look at the Department of Defense once every year, rather than twice every year. If we did it once every year—in other words, that the Armed Services Committee would have a subcommittee on appropriations that would deal with the 1-year's funding; then you would free up time on the floor for dealing with other big issues.

Clearly, what that means is that you are doing away with a committee that has been in existence since right after the Civil War. But there are a lot of other things that we had in place during the Civil War that are somewhat out of date, and we have modernized them. And, yes, people on those Appropriations Committees would have to undergo a difficult transition, but they would all be placed on committees where they would have significant say over major parts of the budget. And then you would be setting the limits and

setting the major goals, in, of course, negotiation with those committees.

Senator PERDUE. I am out of time, so I think we will submit this in writing, if you guys—I would love to have a response to that by the other witnesses, Mr. Chairman, if you do not mind. Thank you.

Senator ENZI. Of course, that is twice now that Ambassador McTigue has not gotten to speak, so I would give little bit of latitude to give him an opportunity to address either of those before we move on to Senator Kaine.

Mr. MCTIGUE. So, very quickly, Senator Whitehouse, you are absolutely right in that tax spending never gets the same attention as normal spending. And part of the reforms in my country abolished all tax spending and put all of that spending on the spending side of the budget, so there were no back doors for people to get through. It also meant that you are much better able to target particularly social spending at the thing that you needed most.

And, Senator Perdue, your comment about outcomes and some of the experience on outcomes, one of my portfolios was to be the Minister of Employment, and when I became Minister of Employment, I inherited 34 programs. And when we audited those programs to see how good they were at putting people into work, we found that four worked really well and the others were mediocre to total failures.

So what we did was that we decided that we would terminate 30 of those programs and concentrate on the 4 because they showed the best outcome results. In year one, we got 300 percent more people into work for 40 percent less money. This is not an unusual order of magnitude change.

Now, what we are really talking about there is maximizing the public benefit with the money available, and you cannot do that unless you line up all of the programs together and check one off against the other and say here is the best, that is where we should make our major investment.

Chairman ENZI. Thank you.

Dr. Posner, did you want to complete—again, if Senator Kaine does not mind waiting just a moment.

Mr. POSNER. I would just say in some respects, what the budget process was, was an experiment, the 1974 act. Can Congress maintain a shadow committee that does things a holistic way, that has as totally different orientation to spending? And I would say right now the answer is probably not. And I guess what I am urging in this testimony is to test the system, and let us test that proposition. Can the Budget Committees become a catalyst to organize Congress in a different way around these reviews? And if not, then maybe it is time to think about taking the blueprint out and restructuring the whole thing, which obviously has lots of questions and issues.

But that is the proposition that Congress put forth in the 1974 act and did some useful things, like creating CBO and ultimately reconciliation. But we never really tested whether this Committee can do program review and oversight in a holistic way. That is what I think we could do.

Chairman ENZI. Thank you.

Senator Kaine, thank you for your patience.

Senator KAINE. Well, this is very interesting to me, and I have got two George Mason faculty members with a connection to Virginia, so I am not going to be rude to them. I am going to be very selective—

Mr. MEYERS. Uh-oh. [Laughter.]

Senator KAINE. Let me just say thanks to all the witnesses, two George Mason connected, and the Maryland guy mentioned one of my gubernatorial initiatives, Virginia Performs. So I am glad to listen for a long time.

Just on George Mason, my father-in-law, when he was Governor, signed the charter to create George Mason as a separate university. It had been part of the University of Virginia. And there was a ceremony yesterday on the campus to name a quadrangle there after my father-in-law, who is now 93. And he was there and very proud, so he feels great connection with the university.

I really appreciate the way the Chair has put sort of reform ideas on the table for us to grapple with. I have enjoyed being on this Committee as a new Senator because I think, admitting all the challenges of the budget process, it is a great Committee to be on when you come into the Senate to kind of get a holistic view, a little bit of the big-picture view, and yet the process has problems.

Yesterday in Foreign Relations, Chairman Corker just kind of went off on the budget process, you know, because he is a member on Budget as well, and just how disconnected it is when you have budget and authorization and appropriation.

But we have had a couple of, I think, very good discussions here about reforms. Biennial budgeting—I would acknowledge that is an incremental, not a, you know, dramatic improvement. But I was with the National Park Service employees Monday in one of our biggest national parks, Shenandoah National Park, and they were saying, “Thanks for the 2-year budget.” Even with a 1-year appropriation, a 2-year budget gives some certainty. Once that first-year appropriation is done, you kind of understand the range where you will be for year two, even though it is not a second-year appropriation. But I thought it was interesting that NPS leadership—and I have heard the same thing from military leadership serving on Armed Services, “Thanks for the 2-year budget.” Compared to the CR or the sequester or the furlough or the no-budget, the idea of a 2-year budget, even with 1-year appropriations, is something that they appreciate the certainty. And I think it helps us on the private sector side, too.

I wish we had a debt management product. Nothing is more annoying, I know, to Senators than people who come in and they have been mayors and Governors and they think they know how to run things. But every city and county and every State has a debt management policy that usually is we do not worry about the debt number, the raw number, we worry about ratio of debt to GDP or debt service payment to the entire annual outlay in a budget, and we do not have an agreed-upon debt management policy.

In Virginia, and other States, there is an agreed-upon policy. And then there is vigorous partisan debate about how to get there. Do you cut expenditures? Do you raise revenues? What do you do? You end up with all the room for the vigorous argument between the parties that you have. But you kind of have a bull’s eye that you

are shooting at, and we do not have that at the Federal level, and the hearings that we have done here have elucidated that.

Then, finally, the issue of performance data, which is covered by some of your testimony, and, Dr. Meyers, your point, Virginia Performs, we basically just decided when I was Governor to create a website that just tracked the key performance measures about whether the State was succeeding or not—not State agency missions, you can drill down to get into it, but unemployment rate, you know, graduation rate in high school, maternal health, infant mortality. And every measure, we put arrows. You know, it is an up arrow if it is getting better. It is a flat arrow if it is not changing. It is a down arrow if it is getting worse. That drove a lot of our spending decisions. When we had more money to spend, we looked at that to decide where to spend. And when we had to cut, sadly, we also—and my 4 years was all cutting. We looked a lot at that to determine where would we cut, that we were really cutting for tomorrow than today. And I think the idea of incorporating more performance data and caring about performance as part of budgeting is key.

On the idea of portfolio budgeting, I am kind of a certainty freak because I just think the more certainty we provide, the better off everybody is going to do. And I actually think the American economy is pretty strong, but there is still uncertainty, and Congress has been one of the great generators of uncertainty, because if it is not clear whether we are going to have a budget or a CR, is there going to be a shutdown of Government? Is there going to be a sequester, partial sequester, full sequester, sequester relief? Are we going to furlough employees or not? That not only creates all kinds of challenges within the organization, and it takes Pentagon planners who should be planning what to do about, you know, a North Korean nuclear program and makes them spend time running five budget scenarios instead, but it also creates a lot of angst out in the private sector, which is the big part of the economy.

So talk to me about how portfolio budgeting could enhance the certainty effect. I want us to provide more certainty, not less. Talk about portfolio budgeting and certainty.

Mr. POSNER. Well, I think the point is that Congress needs to step up to the plate and have a budget resolution and an agreement and appropriations. I mean, that is the bottom line. I think portfolio budgeting helps Congress better find ways to express policy preferences without loading it all on to discretionary. The political debate is focused on discretionary as a proxy for the size of Government. Well, the size of Government is determined by mandatory spending and how many tax preferences you have in that Tax Code, which collectively now equals more than discretionary spending. We have \$1.6 trillion of tax preferences. The discretionary process just collapses, and we end up with these, you know, terrible funding hiatuses.

So I think if you could think about budgeting like the States do, that everything is in play. You reach agreement at the front end about some big pieces you are going to go after every year, I think that would start to structure the debate better and take some of the burden off of the discretionary side.

If I can add one more thing about debt, before I came to George Mason, I led GAO's work on the Federal budget for 15 years, and we did some studies in New Zealand and places like that and looked at a different way to think about debt limit, because we thought the debt ceiling is a horrible way to do business. It is an after-the-fact thing that is always destined to fail. And New Zealand came up with, I think, a better mousetrap, which is they articulate the debt as a share of GDP as a target, and at least when we were there, for a good 10 years, all political parties observed that target as kind of a line they would not cross. And I thought that was the kind of thing we should be looking toward—because that is a prospective target that guides future policy. The Committee for a Responsible Federal Budget issued a report back in 2010, that included a long-term debt target that we should be striving for as a matter of policy.

Senator Kaine. Well, if I could—and I am going to ask a question, but just back to the Chair—and I am sure that your city, when you were mayor, you had exactly the same thing. Well, you had a no-debt policy, if I remember correctly. We had a debt policy. We were a double-A city. We were a triple-A State. We want to maintain double-A and triple-A, so there were bonding agencies to answer to. But we had, you know, basically two measures: debt as a percentage of State or local GDP and debt service payment as a percentage of the annual budget.

What is interesting, it was not a mandate. There was not a law that says it can never exceed. It was just an agreed-upon framework, this is what we are going to try to have. And if we needed to go over it for some reason, well, we better have a real good reason. But we usually did not. But it preserved all kinds of room for partisan debate about how to get there. But it is very challenging to—and the debt ceiling is so artificial in so many ways, it is looking backward. And it is a raw number, and the raw number means nothing. It is the ratios that have economic value, not the raw number. I mean, if you say \$17 trillion, of course, people go, "Oh, wow, that is incredible." But \$17 trillion could be the perfectly appropriate level of debt, depending on the size of the economy. So the raw number is meaningless, and yet we use that instead of really having a meaningful policy.

I am going to look at that paper because I would like to see, you know, how you might approach that. And we will have plenty of room to argue about how to get there, but not even having a target to shoot at I think is challenging.

So good testimony and a good hearing. Thank you, Mr. Chair.

Chairman ENZI. Thank you. I should correct, we did have debt. It was debt for infrastructure. But it had to have a dedicated revenue source before we could enter into that.

Also, I would mention that I do not do any town hall meetings. I only do listening sessions. That means I go to a town, somebody introduces me, and we have a microphone, and I do not make any comments. People come up to the microphone one at a time and tell me what I need to know. And I take notes as they are doing that, and if I see something or hear something that I really think is significant, I circle it so it will be a little easier for me to find in my notes. And then when the listening session is over, I answer some

of the questions that people raise, but they do not get rebuttal at that point, and there is not any further testimony that gets to do a rebuttal on it either. But I mention some of the ones that I have circled as great ideas that I want to haul back to Washington again. And I have got to say that that is still the way that I take notes, and I cannot believe how many things I have circled today because of your testimony and because of your answers to questions that have been posed today. And Senator Whitehouse's opening speech had a number of things that I circled as well. I think there is a lot of common ground for a common country that we need to achieve.

So I do have some questions, and I will start with Ambassador McTigue. The Government Performance and Results Act, as it has been amended, already requires the agencies to produce data that measures programs' effective in relation to desired outcomes. How could we change the process to improve the use of this information?

Mr. MCTIGUE. The simplest change in my view would be that at the time of making the appropriation you added another paragraph that described what benefits you would have received from this appropriation a year from now or 2 years from now, and then oversight would look at that number and decide whether or not you did well.

Now, if you missed the targets, it might be that you are buying the wrong programs, you are making investments in the wrong tools. Or it might be that you just need to put more resource into it, but it does give you something that you can actually use and you can make progress.

The second thing that it does is it also tells you some of these tools do not do anything to touch the outcome. I will just give you a very brief description.

If somebody is hungry and I feed them, that is a good thing to do. And if I feed them tomorrow and the next day and so forth, it becomes a less good thing to do because I am not looking at the real problem, which is their dependency. Why are they hungry? And I have got to address those things that are making them hungry to be able to get a successful conclusion. Maybe they cannot read or write. Maybe they do not speak the language. But at the same time as feeding them, I should address those things so that at some stage I will not need to feed them anymore.

So that is what outcomes do, in my view. It enables you to actually see whether or not you are using the right tools and you are making the right kind of progress.

Chairman ENZI. As kind of a follow-up to that, sometimes we fall into the trap of thinking about this program performance and efficiency as an excuse to cut. But spending more on ineffective programs does not help, and we are perhaps hurting the beneficiaries, as you just explained.

When you implemented the outcome-based budgeting reforms in your country, what effect did that have on the benefits that were provided?

Mr. MCTIGUE. It made us do a lot of things differently. So, for example—I will use an example that Senator Whitehouse referred to before about homelessness. So we used to measure homelessness in terms of how much low-cost accommodation we had put together

and where we had distributed it and everything like that. But when we actually went back and saw what happened to homelessness, we found that the proportion of homeless people was not diminishing.

So we went back and did what we should have done the first time, and that is, research it properly. And when we researched it properly, we found that 70 percent of homelessness is caused by mental health problems, not the unavailability of accommodation. When we addressed that issue, we found that within a year homelessness had dropped by 30 percent and then dropped by another 15 percent the following year. So that is outcomes telling you that you are using the wrong tool, and I think that is incredibly valuable information to have. Otherwise, you are guessing.

Chairman ENZI. Thank you. I will have some follow-up questions with some more detail, but I will do that in writing so you can respond to it.

Dr. Posner, I have introduced legislation to do a biennial appropriations process. There are several proposals that way. Mine puts six appropriations bills each year, but they are for a 2-year period. Then the most difficult ones follow an election, and the easiest ones are just before an election, thinking that we might be able to get through them that way.

Would moving to a biennial appropriations process make it easier for the Budget Committee to work collaboratively when they are authorizing and the Appropriations Committee is doing portfolio reviews? What do you think about a biennial appropriations process? Even the appropriators like a biennial budget process, and we can probably go to that pretty easily.

Mr. POSNER. Well, let me just say that, obviously there are lots of other things at stake. I always used to say, because I was at GAO for 30 years, I am an Article I guy, and I get very concerned about delegating more power to the Executive. But, nonetheless, I think it certainly could accommodate a biennial process with this Committee and others doing portfolio reviews during the off cycle, say in certain of those appropriations that you are talking about. That is the way it worked in Arizona. At GAO we did a study of State performance budgeting back 15 years ago. Arizona had just moved to biennial budgeting, and the leadership agreed to have legislative committees focus oversight on several cross-cutting issues in that biennium. One was juvenile justice, juvenile delinquency program, and several others. And that focused the committees doing oversight to a great extent.

Now, that sounds too neat to be true, certainly may be too neat to describe the Congress, but, nonetheless, that is how you might draw that one up.

Having said that, I think the portfolio process could also accommodate itself into an annual appropriations cycle as well, as witnessed by this Committee's brief use of task forces in 2000. So I think it—but certainly I can see how biennial would help promote that.

Chairman ENZI. Thank you. My time has expired. I will go back to Senator Whitehouse, and we will do another round here if people are interested.

Senator WHITEHOUSE. Thank you.



I guess this is a little bit in the nature of suggestions, but I think if we put together some combination of the McConnell rule, which spares us the debt ceiling crisis, and a debt target of some kind, and some form of consequence, depending on which side you were of the debt target, not necessarily a catastrophic consequence—because as soon as you create a catastrophic consequence, you can bluff your way through it because people really are not willing to pull the trigger on it, and it becomes, like the debt limit, an opportunity for finger pointing rather than an opportunity for work.

So I think that is an area that if we pulled those things together, we might be able to actually create incentives, targets, systems that work on an ongoing basis.

I also think that if we are to start looking at portfolio areas, we might want to think about just agreeing amongst ourselves to pick an example or two and try it out, see how we do, see what we bump into, see whether there are things we learned about what we chose that made it a good or bad choice. I think as I said earlier about cyber, if something is spread across 38 committees, that may be an easier area and more responsible area for us to engage in than if it is defense appropriations that is pretty well squared down into, you know, basically two committees.

So I am open to—and I am sure other members would be—trying to figure out how we might go about doing that. But that takes me back to the question that I left Dr. Posner with, which is what guidance—and this would be for all three of you. What guidance would you have about where and when, given that we cannot look at all the portfolios of the Federal Government, where and when should we direct our first efforts if we are going to embark on first efforts at this kind of portfolio budgeting theory? And I cut you off in mid-question, so let me go back to Dr. Posner.

Mr. POSNER. Well, one of the areas I have talked about here in the Committee before is food safety. We have 15 agencies administering 30 laws. So when there was the salmonella outbreak with eggshells affecting 500 million eggs, it turns out that jurisdiction over eggshells is split, incredibly, between Agriculture and FDA. So FDA monitors the eggshells; Agriculture monitors the young chicks. FDA monitors the feed that is given to the young chicks; Agriculture monitors the transportation. It is an incredibly Byzantine process and one that our agencies heroically try to deal with. Many other nations—and GAO called for a unified food strategy agency, as other nations, long have had a unified food strategy program. Most European nations do. That is an example of one, I think, where—so one of the hallmarks is agreement on goals. Nobody disagrees that we want the most effective food strategy program we can.

There are a lot of areas of policy that are like that. Homeland Security has 16 homeland security grants—the UASI grant, the State homeland security grant, transport security—and, apparently, notwithstanding some previous agreement by the agency, Congress has never been able to see its way clear to bring those together in some sensible way.

So I think there are lots of areas that are target rich where there is broad agreement that you could take—nothing is low-hanging

fruit, of course, but I would think to what extent are the broadly shared goals would be a first criterion.

Senator WHITEHOUSE. Ambassador McTigue.

Mr. MCTIGUE. Thank you, Senator Whitehouse. Just very briefly, another area that might be interesting to look at in terms of a first portfolio might be all of those programs that touch the environment and look at those and see whether or not they have—some have better outcomes than others or they are even measuring the right kind of things.

Can I just go back to what you were speaking about with regard to debt? And it also cross-references to what Senator Kaine had to say.

Senator WHITEHOUSE. I would not mind that, but as my time is going, let me turn to Dr. Meyers to answer my question, and then we can come back to you if the Chairman will permit that.

Mr. MCTIGUE. Okay. Certainly.

Mr. MEYERS. In the paper that Dr. Posner wrote with Steve Redburn, they suggested housing and higher education. Well, since I am a professor, maybe I would say leave us alone. [Laughter.]

But my preference actually would be for health because I think it is such an important area and it does illustrate some of the challenges with moving across discretionary, mandatory, and tax expenditure.

But I think it is important to realize that in one sense you already have portfolio reviews at some level—you have authorizations on a multi-year schedule for some areas of the budget—ag, transportation, and so on. And those could provide a clue for how you might envision moving from an experimental portfolio to a new or regular order, which would be for each sector of the budget you would have a sunset schedule, and every, say, 4 years or so, you would have a reauthorization, and it would be supported by having a QXR, as I would call it, a quadrennial review for that sector of the budget given to you by the executive branch that would help you structure things.

The other relevant point, I think, is that there are some programs you do want to put on autopilot or at least close to it, like Social Security. You want to review that program periodically, not every year. And there are other areas where you want to keep the agency on a short leash every year. So, in fact, you want diversity in terms of the frequency in which you evaluate programs with a fine-tooth comb. But you also do want some diversity within each sector because, you know, America is a diverse country; we do need to reduce overlap and redundancy, but in most areas it is hard for me to imagine that there would be a one-size fits-all program that would be satisfactory to all Senators and Representatives.

So, take advantage of our diversity, but figure out a new structure in which you can promote that diversity and get rid of unnecessary overlaps. You can think about what is the need to keep some programs on a short leash, evaluating them frequently, and then how can you look periodically at those long-term commitments that are central to our policy and society, to make sure that they do not get out of control.

Senator WHITEHOUSE. Thank you.

Chairman ENZI. Senator Kaine, do you have some more questions?

Senator KAINE. No.

Chairman ENZI. Okay. Ambassador McTigue had some additional comments, which is the direction I want to go with my next questions, too.

Mr. MCTIGUE. Okay. The comments from two or three sources about how you manage debt and whether or not you should manage debt, well, the worse results come from a process where debt is an accident of the decisions made in the budget, and you can see that in many countries around the world.

One of the innovations that I think is very interesting is places like the United Kingdom and New Zealand, they take budget strategy and budget policy out of the numbers part of the budget, and they issue the documents on that 6 months ahead of the budget. And that deals with things like debt policy. So what are going to be the targets looking a long way forward? In 2012, New Zealand set a debt target of being under 20 percent of GDP by 2020, and it will be there. And the United Kingdom set one of having a budget surplus by 2020, and it looks like it will be there. So that strategy being set ahead of the budget numbers I think gives better resolutions.

The other thing is that those countries also, while they have annual budgeting, they give firm numbers for the out-years. So when the British budget comes down, you know what the numbers are going to be for the next 4 years as well. So that gives the certainty that Senator Kaine was talking about. In New Zealand, you are 3 years—3 years are firm numbers. You get a projection for 10 years, and you get a speculation for 20 years out.

Now, nobody really gets held to the 20 years ago, but sometimes if you look that far ahead, it shows you the consequence of a decision that you have just made when it gathers full momentum, and that can have consequences that you did not expect unless you have a very long term view looking forward.

Chairman ENZI. Thank you. Continuing on the ways to handle the debt, does anybody have a formula that factors in the cost of interest? This is kind of a worry to me because right now at 1 percent we are spending \$230 billion a year for our debt, and the norm is 5 percent. But if we happen to go to 5 percent, we would be spending \$50 billion more than we get to make decisions on right now, which means no defense, no ag, no commerce, no education, no everything that we do—unless, of course, we dip into the mandatory programs. And, of course, we have gone from 30 percent mandatory to 70 percent mandatory, and I have even suggested maybe we need to go to 100 percent mandatory. Then we would actually have to make some decisions, and people would realize the impact of the mandatory things. Or we could go the other way and make nothing mandatory. But probably neither of those is going to work.

But does anybody have a factor in—of how the interest would work in this debt management formula?

Mr. MCTIGUE. A very brief comment. Part of the debt management strategy looks not just at the total quantity of the debt, but the cost of maintaining that debt and what it will be over time.

And that triggers the decisions about how much of it you are going to pay down in the medium and the longer term so that you are in a position to be able to withstand shocks when they occur. And I think most of the world has become very much aware of if you are living right on the edge of the cliff and you have something like the Great Recession, you have terribly big problems. And getting back from the edge of that cliff quickly is a prudent strategy. That needs to be part of the budget process, and I do not think there are too many discussions about that here in Congress at the moment.

Mr. MEYERS. In its annual outlook report to you from CBO, that information is presented to you. It shows the interest increases that would result from one budget path as opposed to the other. So that information is available. There are two difficulties: One, comparing the U.S. to New Zealand is that we are too big and rich to make debt worrisome to us until it becomes too late. In New Zealand's case, they made those big changes because they had serious problems in their balance of payments. So we have this exorbitant privilege, as Barry Eichengreen, the Berkeley economist, calls it.

But the other issue is; how do you connect that medium-term debt target, which I think we all agree is a good idea, to specific policy choices that you make? And that question is one reason why biennial budgeting or some longer-time perspective is useful. Not only does biennial budgeting give certainty, if it is at the appropriation level, to agencies, since you really do not expect their needs to go up and down too much from year to year, but it also allows you to have a medium-term glide path towards that macro policy result that you want.

But, again, that gets back to the central point of this hearing: How can you structure your budget process so that you can sift through those programs, get rid of the unneeded ones, and also throw money at the ones where there are a lot of promising ways of making America's lives better, that is consistent with your budget targets? This was the challenge that was faced in 1974 when Congress passed the initial Congressional Budget Act, and actually, there were some good years in that history. You and the President made progress during the 1990s.

So now you are faced with this difficulty. You are absolutely right that debt increases are worrisome over the long run, and I think a lot of people are looking to you for leadership, to come up with new ideas for how we can address that problem more fruitfully than we have in the last decade or so.

Chairman ENZI. Dr. Posner.

Mr. POSNER. The Canadians at one point singled out the interest. They had a target called "interest bite," and they were concerned because their debt ultimately grew to 100 percent of GDP. And it was the interest, of course, that shows up in the annual budget and crowds flexibility.

And so that became a big issue in public policy and whether that is something that could be highlighted.

On Ambassador McTigue's point, I want to suggest that the main point of the budget resolution was to force Congress to go on record about something they had not been on record before, which is the size of the deficit, the size of the surplus, whatever it is going to

be. But that is obviously not the only thing that matters, and I think what Dr. McTigue is pointing out here is that thinking more about the long-term targets and how they might be reflected in the budget resolution is also something that is worthy of your consideration. And, again, in the 2010 report that we did with the Committee for Responsible Federal Budgeting—I think it was called “Getting to Black”—we talked about how the budget resolution could be a vehicle for Congress to articulate what its debt target as a share of GDP might be. So going beyond just annual deficits, which is very limiting, forcing Congress to think more long term is part of this prospect.

Chairman ENZI. Thank you.

Do you have some other questions you would like to ask?

Senator WHITEHOUSE. I just wanted to thank you, Mr. Chairman, for leading this Committee into this area. I think we have an enormous amount of work to do, and I think we have to be very prudent about what we set before ourselves so as not to be overwhelmed either by jurisdictional concerns from other committees or leadership concerns or other such things. But I think the prospect of a better-run Committee, a less foolish vote-a-rama, a longer perspective that drives us towards a more responsible management of our debt, and some opportunity for being a portfolio reviewer are all very useful and valuable things, and I am confident that there would be good bipartisan support for working towards those.

I think you and I probably agree that if we are going to pick portfolio areas, they should be less hyper-charged than environment and health care are right now. But maybe the day will come when those would be areas we could look at. But I think right now we would step into food fights that we do not need to step into. And with that, I again thank you very much for your leadership.

Chairman ENZI. Thank you. Thanks for your participation and good suggestions, and I particularly like your suggestion that maybe we needed to try one or two areas of portfolio first to show that it works. Then we can get into the more controversial ones. And I think they can work, too. Neither side is going to get 100 percent. I have got this 80-percent rule that I have worked under where there is usually common ground of about 80 percent. But there is 10 percent on each side that we are going to fight to the death on, and, unfortunately, the fight to the death winds up with the issue dying, not the people—well, fortunately, I guess. [Laughter.]

But that 10 percent on each side are going to be around. What we need to find is that middle ground of the 80 percent, and we can get it done. And I think this is an opportunity for us to do some major things here. As you know one of the things I have been disturbed about for the whole time that I have been here, not just recently, is that the President’s budget really is not looked at by anybody, but the pages are about that thick. And I know that there are 535 copies distributed to the Members of Congress and the Senate. But I think there are several copies that are delivered to the staff as well, and anybody else who wants one, although I am wondering if anybody has ever looked through all of those pages. It would be real helpful if it were on a disk so it would be searchable, but one of the things that was mentioned here today is making us

a committee on national priorities and getting an annual report on the true state of the Nation. That would really be helpful by a President.

Another suggestion that we have had here is something that goes for 4 years. Well, the only thing that we have that goes for 4 years is the President, because the House goes for 2 and the Senate goes for 6, but the President goes for 4. And the President has a huge influence. He is one third of our structure of Government, and so when he comes into office, he ought to be presenting us with what he wants to get done during that 4-year period. And then we as the Budget Committee can set some national priorities and hopefully some formulas for what kind of target we are going to have on debt and get the committees to work from that standpoint.

But those are all very major changes, and any change around here is difficult. We are supposed to be the inventors of everything, and we are really the continuers of everything.

I was going to ask some questions about unauthorized programs because that has been a pet peeve of mine. My first year as the Chairman, I discovered we had 260 programs that had expired that we were spending \$293.5 billion a year on. And I hammered on that enough, obviously, that there was some attention paid to it, because we have gone from 260 of them down to 256 now. But we have increased the spending to \$310.4 billion. So our priorities are not working out real well. And I will have some more technical questions for our people on that.

I was also intrigued with the comments we had on the reconciliation instructions, and they need to be a bit more effective and not just a tool for pushing through the 10 percent that one party or the other cannot get done any other way. And we also need to have the President involved earlier in the budget process so that we do not wait until November to force an issue and disregard what we did—well, not totally disregard, but almost totally disregard what we did. So we have got to find it to be an effective tool, and we have had a lot of good suggestions here today, and hopefully other members of the Committee will submit some questions. But above that, I hope they will just read the testimony that you have already presented. It was well put together, and I appreciate all the effort that went into that.

So thank you, and we hope we can call on you again as we develop some of these ideas to see if you think they have got any merit or if they ought to be revised some way.

So thank you very much, everybody. Thanks.

Senator WHITEHOUSE. Thank you, Chairman.

Chairman ENZI. The meeting is adjourned.

[Whereupon, at 12:05 p.m., the Committee was adjourned.]

“Budgeting For Outcomes to Maximize Taxpayer Value”  
 Senate Budget Committee Hearing  
 April 13, 2016

Responses to Questions for the Record

Dr. Paul Posner  
 Director, Center of the Public Service  
 School of Policy, Governmental Affairs  
 George Mason University

#### Questions from Senator Stabenow

**Question #1: Can you go into more detail on how portfolio budgeting can help Congress even when the goals and policy solutions are very different? What additional steps would the committee need to take to ensure that portfolio budgeting worked?**

Portfolio budgeting is designed to be used selectively. It would likely be more useful in cases where the selected policy area is one where there is broad agreement on the goals of policy, even if there is no agreement on the best way to use resources to achieve them. Higher education provides a good example of such a policy area: there is broad, if not universal, agreement that the federal government should help expand access to higher education that will lead to better employment and income but not excessively burden students or their families with debt. There is much less agreement on how well current spending and tax policies are working to achieve this or on what alternative set of policies might yield better results at the same or lower cost to the budget.

To be effective in such circumstances, it would help if the budget committees were to identify a small set of major policy areas where there is general agreement about policy objectives, dissatisfaction about current policies, and evidence suggesting that federal spending, tax policies, and other policies could be altered to use resources more productively. GAO’s annual report on overlapping, fragmented, and duplicative spending is one source to consider.

Chairman Enzi’s recent outline of his budget reform proposals included a provision to provide the budget committees with authority to establish subcommittees to review spending and tax policies constituting the relevant portfolios for selected policy objectives. The budget committees would have to consult extensively with leadership and other relevant substantive committees in reaching agreement on those vital few areas ripe for a portfolio review and oversight

A step the budget committees could take in this direction would be to form a partnership with the Executive Branch to conduct research and define policy alternatives. The executive agencies are required to consult with Congress on

strategic goals as mandated by the GPRA Modernization Act of 2010 when they develop their next strategic plans. Those consultations, which should occur next in 2017, could help identify policy areas ripe for portfolio review. At the start of a new administration and Congress, parallel leadership-level discussions might be held between leaders of Congress and the new White House to identify policy objectives that would be the focus of analysis and special attention in the FY 2018 or 2019 budget process. This does not presume agreement at the outset on policies, only a shared recognition that review would be timely and potentially productive. It would be helpful if these discussions led the Administration to conduct its own portfolio reviews on these agreed upon areas during the President's budget process. The Budget Committees could then follow up on these Administration reviews by doing their own analysis and review, informed by the conclusions and recommendations of the Administration.

**Question #2: How does your portfolio budgeting proposal address tax credits and programs that have effects on multiple budget portfolios?**

Analysis of the portfolio of policies – including spending programs and tax policies – relevant to one policy area should include estimating the full range of their effects. While the focus of a portfolio review would be on the impacts of proposals on policy goals of a discrete substantive area, a good analysis would have to also reveal other consequences of recommendations for other policy areas. As you suggest, an expansion of EITC might very well have effects across a number of relevant policy goals that should be revealed. In the case of higher education policy, this might include estimating effects such policy objectives as reducing inequality or promoting economic competitiveness.

**Question #3: Where else has portfolio budgeting been implemented, and what are the lessons learned?**

A number of other nations conduct in-depth spending reviews on a selective basis as part of their budget development. Many nations have learned from the Netherlands which has been doing these reviews for at least twenty years. The 2010 spending review examined 20 topics and was designed to produce options to reduce spending by 20 percent over four years. In years when the budget was not in deficit, spending reviews were conducted as well, focusing on performance rather than savings targets. So-called Interdepartmental Spending Reviews have been ongoing since the early 1980's, featuring a review of policy arenas that cut across ministries. These initiatives have often included not only Finance and line ministry staff but also outside experts and have led to significant savings over the years. Tax expenditures have been included as part of these reviews where tax subsidies play an important role in achieving program goals.

In a review of the experience of other OECD nations, a report this author led found that these spending reviews were productive of reform and innovation in individual policy



and program areas across the board.<sup>1</sup> For instance, the UK 2010 spending review prompted the Ministry of Justice to abolish their regional structure, introduce private financing under a social impact bond for rehabilitation of offenders and increase partnerships with private and voluntary sectors in counseling with prisoners.<sup>1</sup> Senior budget officials also attributed other reforms to the spending review including the shift of higher education from grants to loans, reforms to disability programs, public pension reform, among others.

Denmark achieved major reforms in policing, defense management, tax administration and primary school teaching from this process. Moreover shared services initiatives that have increased efficiency for back office management functions also stemmed from these reviews. Senior budget officials remarked that, notwithstanding the breadth of these proposals, the recommendations were most often accepted. The involvement of key stakeholders in the review process helped promote support across affected interest groups.

The states have also sought to implement budget prioritization initiatives that compared the relative performance across related programs across the entire budget addressing common performance goals. In early 2000, Arizona, for instance, developed a strategic performance review where legislative agencies undertook crosscutting performance reviews of government services that spanned several programs and agencies. More recently, states have followed the lead of the State of Washington to institute cost benefit analysis of comparable programs, which has resulted in changes in budget priorities in discrete policy areas. The Pew Foundation has supported a 22 states in building the analytic and information infrastructure to support a similar process facilitating the more systematic comparison of competing claims within state budgets by legislatures. New Mexico used this approach to compare the return among programs in criminal and juvenile justice, child welfare, and other key policy areas. The state, through its budget process, directed \$104 million to the most effective programs. Moreover, the New Mexico Corrections Department adopted a policy last fall that commits the agency to maintaining an inventory of its programs and mandates that 70 percent of funds be directed to evidence-based programs. The new Evidence Based Commission enacted by Congress is designed to build on these state based laboratories to improve the data and information basis for federal budget decisions.<sup>2</sup>

These state initiatives are notable and have achieved improvements in evidence based decisions. However, the more sophisticated information must be accompanied by the development of budget institutions empowered to make decisions across competing programs, agencies and committees to arrive at more cost effective policies. Some states are positioned to do this because they have more cohesive and integrated legislative

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<sup>1</sup> Paul L. Posner and Tim Higashi, *The Role of the Budget Process in Promoting Public Sector Innovation*, June, 2016.

<sup>2</sup> <http://thehill.com/blogs/pundits-blog/uncategorized/281321-feds-can-learn-lessons-from-states-about-using-data-to>

institutions and committee structures. The question is whether Congress can follow their lead.

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## **TAP DANCING ON THE RAZOR'S EDGE: RESTORING STABILITY TO GOVERNMENT OPERATIONS**

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**WEDNESDAY, APRIL 20, 2016**

U.S. SENATE,  
COMMITTEE ON THE BUDGET,  
*Washington, D.C.*

The Committee met, pursuant to notice, at 10:30 a.m., in Room SD-608, Dirksen Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Crapo, Ayotte, Corker, Perdue, Murray, Stabenow, Whitehouse, Baldwin, Kaine, and King.

Staff Present: Eric Ueland, Republican Staff Director; George Everly, Chief Council; for the Minority: Joshua Smith, Budget Policy Director.

### **OPENING STATEMENT OF CHAIRMAN ENZI**

Chairman ENZI. Good morning, and welcome to our latest hearing in a series that this Committee is holding on America's broken budget process.

For a country that is exceptional in so many areas, it is simply inexcusable that our budget process has devolved to its current state. There is growing consensus that our Government needs to change the way it makes funding decisions, and this Committee and its members have a unique opportunity to lead that effort.

As we have seen, the current process is designed to fail. It is time to make the process fit the problem. Even small changes can begin to reform the budget process so that it will have a better chance to succeed. Such improvements can in turn help our country succeed in addressing runaway federal spending and our exploding national debt.

Budget process reform is not a cure-all. It will not fix all our budget problems. But that does not mean we should resign ourselves to muddling through under a budget process that predetermines failure. I would like to work with my colleagues to propose fixes that encourage transparency, accountability, and an effective and efficient Government.

Last week, expert witnesses explained that the budget decision-making process does make a difference. Fragmented decision-making has caused duplication and waste that actually diminishes the value of the public services provided to our constituents. Today we will hear about other costs resulting from budget dysfunction

and, more importantly, explore solutions that might inject stability into the process.

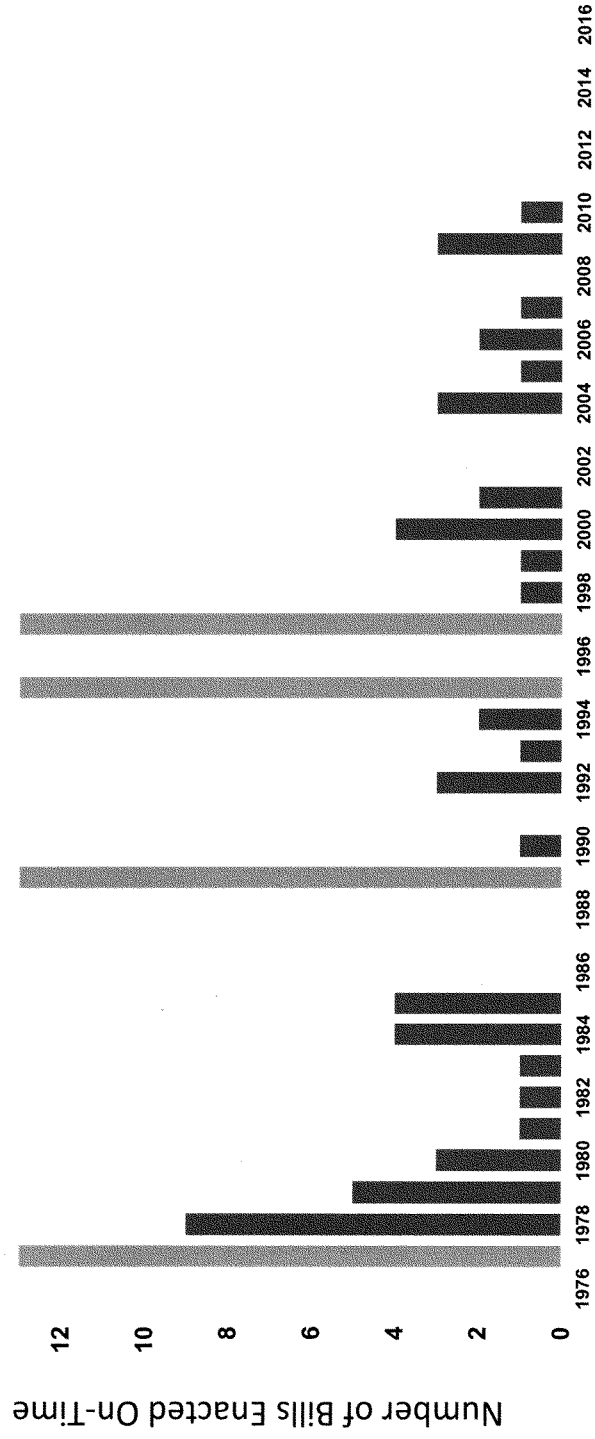
When Congress fails to establish predictable tax and spending policies, Federal agencies, State and local governments, private organizations, and constituents all pay the price. Nearly every aspect of the current budget process is riddled with uncertainty.

For example, the annual budget resolution could serve as a long-term planning document that signals to stakeholders how Congress will allocate the country's limited resources. Instead, it currently bears little relation to the tax and spend decisions Congress must make every year.

The annual appropriations bills are chronically late and have not passed through under regular order in over 20 years. The chart on the screen shows how timely the appropriations process has been since the Budget Act of 1976 took effect.

The green bars represent the four times that Congress has completed appropriations on time in the last 40 years. The red bars represent progress toward that goal. You notice that zero appropriations bills have been enacted on time in the last 6 years.

# **Congress Completed Appropriations On-Time Only 4 Times in 40 years**



I commend Leader McConnell's effort to move the fiscal year 2017 appropriations bills under regular order this year. But it is a challenge working against a system that in its current form makes it nearly impossible to accomplish the task.

There is also significant uncertainty generated by the Government's future overspending. The Congressional Budget Office says the Government's continued overspending will add \$11 trillion, which is 11 thousand billion, in additional debt in the next 10 years as entitlements begin to take over the budget. If that is not alarming enough, the annual interest costs on our debt alone will total \$839 billion per year in just 10 short years, and that is even using a very conservative interest rate.

We simply cannot continue on this course, whether the result is huge tax increases, drastic spending cuts, or some combination of the two. Somebody is going to pay the price. Without a long-term enforceable budget and predictable fiscal policy, Congress is forcing this future uncertainty onto public and private organizations that are trying to plan for the future.

The statutory limit on Government debt should be a warning to Congress of the irresponsible decisions we are making and the country's growing mountain of debt. But this important tool is completely disconnected from our tax and spending decisions. Instead, it occurs well after the fact and serves only to rattle financial markets and increase uncertainty across the economy.

Whether it is the unenforceable budget, whether it is late appropriations, whether it is growing deficits, whether it is impending debt limit showdowns, the uncertainty created by our broken budget process carries severe and indirect costs. Budget dysfunction causes wasteful spending, disrupts Government operations and planning. It also affects the private sector, reducing productive investment and hiring.

Effective solutions will reduce flashpoints for crisis politics and encourage certainty in the budget process. An effective long-term budget would signal future tax and spending levels. It would enforce long-term spending discipline so that the agencies, the businesses, and the constituents can plan accordingly. And it would bring the President into the process so that veto and shutdown threats are less common.

Senator Heller recently sent a letter to this Committee asking us to consider legislation that would prevent Members of Congress from being paid if we fail to adopt a budget resolution and all 12 appropriations bills on time. He is right to focus on incentives and consequences. When Congress or agencies do not act in a fiscally productive manner, there ought to be consequences—not necessarily the consequences in the Heller bill, but there ought to be consequences.

At the agency level, Government managers should be held accountable for performance. Of course, that would require stated, measurable goals. Inadequate results should trigger increased scrutiny and program review. Real consequences for poor performance will improve outcomes for constituents, as we discussed last week. A longer appropriations cycle will also reduce uncertainty. If Congress enacted 2 years of funding and appropriations bills, agencies could plan for 2 years rather than 1 year, and they could spend less

time formulating new budgets and worrying what Congress will do in the next fiscal year. And that is without even talking about continuing resolutions that go beyond the beginning of the year when they do not know what they are going to be able to spend.

Members on this Committee have other ideas on how to improve certainty and reduce crisis budgeting. For example, Senator Portman has introduced legislation that would prevent Government shutdowns by creating an automatic continuing resolution that would take effect when no appropriations have been enacted. And it would encourage Congress to do its job on time by automatically reducing spending until all full-year appropriations are enacted.

No change is easy here in Washington, D.C., so fixing a congressional budget process that has been in place for 40 years may seem like a Herculean task. But this election year gives us an opportunity to consider proposals that do not favor one party or the other. Nobody knows who will be in charge of the Government next year, so our solutions can focus on creating a transparent, accountable, reasonable, and predictable budget process.

Senator Whitehouse.

#### **OPENING STATEMENT OF SENATOR WHITEHOUSE**

Senator WHITEHOUSE. Thank you very much, Chairman, and thank you for your continued focus on how to revive the Budget Committee into a meaningful body here in the Senate. I appreciate the return of Dr. Hassett and Dr. Joyce and Dr. Ornstein, all of whom have been before this Committee before to help guide us through this conversation.

The topic today is budgeting by crisis, and I would suggest that budgeting by crisis happens when obstruction becomes the rule, and obstruction tends to become the rule when people and politics seek to use leverage to gain things that they could not achieve through regular order, essentially budget ransomware.

That problem, which has been our problem for a number of years, is compounded by the 60 votes problem, which is that the threshold that has to be met if you depart from the budget is 60 votes. And particularly since Majority Leader McConnell came to the leadership of the Republican Party, 60 votes have really been the rule in the Senate. So if 60 votes is the rule for anything meaningful in the Senate, then 60 votes is going to be the rule for appropriations in the Senate, and that means you have got your 60 votes for your appropriations, so you do not care what the Budget Committee did. You are through the firewall that violation of the budget was intended to create.

The third point that I will mention is that when the budget is disaggregated from the appropriations accounts, it tends to lend itself more to theater if you actually had to take a budget and start to drill it down and at least show how it would work across the accounts. Obviously, we could not bind the appropriators. But if you actually had to walk through the consequences of a proposed budget, I think that would help take some of the theater out of this exercise.

The last thing I will say is that we are proceeding this year without a budget. The Committee is not going to act on a budget. I

think there is a reason for that, which is that we have an overarching agreement. One of the things that happens when you are budgeting by crisis is that a little group of people go into a little room, and it is the White House and it is the leadership of the Senate and it is the leadership of the House, and they cut some deal, and who ever knows what side deals were cut to make that other deal possible, and it is not transparent, and this Committee has no role in it, and it is not a good way to do business. However, once the deal is done, it is the deal, and it does, to a significant degree, moot the job of the Budget Committee.

So we had to listen to Leader McConnell saying that if he were in charge, we would be passing a budget every year. The law says pass a budget.

We had to listen to Senator Cornyn saying, "When Republicans regain majority in the Senate, we will pass a budget."

We had to listen to Senator Grassley saying, "We have been hitting the Democrats for 3 years that they have not adopted a budget."

Senator Blunt bemoaned a Senate with no budget.

Again, Senator Johnson said not passing a budget is a "national scandal," "hopefully the American people understand what a national scandal this is."

Senator Portman chided us Senator Democrats for neglecting one of our most basic responsibilities.

Senator Ayotte said we were incredibly foolish, the Senate Democrats, that we did not want to do the basics for our country.

Senator Toomey said we were failing in our statutory obligation and an obligation based on decency to do a budget.

And Senator Byrd said, "If Congress cannot pass a budget, then we should not be paid."

So there was a lot of drama when under similar circumstances the Democrats did not pass a budget. I am not going to repay the favor at this point because I do not think that, frankly, we are doing much wrong when we do not pass a budget when we actually are operating in a year in which the budget has already been agreed to.

I think what we need to do is to look back at the process by which that global budget was agreed to. And very few good things happen in Washington in crisis, under pressure, in a room in which there is no transparency, and in which the rest of us as Senators, at the end of that, it is brought out to us and said, "Here is the deal, up or down vote." And, by the way, there is no down vote here. There is no alternative. We are just handed the thing.

So rather than revile each other over not passing a budget, I think the sensible thing to do is to look back at how we make this process work. And the only transparent way you get to a budget is through this Budget Committee. So if this Budget Committee is a nothing, which it more or less is right now, then we are not going to have transparency. And the appropriators are going to run the show, and they are going to make the decisions. And they will roll through any budget because they will have the 60 votes, and that is going to be what continues.

So the Chairman's focus on this to try to remedy the process behind it I think is commendable and I think puts us in a better posi-



tion than pointing fingers at each other, whether we did or not pass a budget in a circumstance in which the budget was already agreed to.

So thank you, Chairman.

Chairman ENZI. Thank you. And I think one of the challenges for this Committee, we have a little card that is here that outlines some of the points of order that can be taken against things as they come up, which, of course, as you point out, only takes 60 votes to overcome it. But my hope is that we can stay with the November deal. I think there will be a lot of opportunities to violate that, and that is going to be my major task this year—well, that is going to be my secondary task because my major task is to come up with some reforms that we can agree on that will actually do what you said: provide the transparency and make this a very meaningful Committee that will help to set some national priorities.

Senator WHITEHOUSE. And I would note for the record that under the Chairman's leadership there has been considerable bipartisan support and interest. We do not have agreement exactly on what, but there is certainly significant agreement that something needs to be done and that in good faith there is a lot that we can do together. So thank you.

Chairman ENZI. Well, I think we are progressing toward coming up with the solutions and then getting together and seeing what we can actually accomplish.

Senator WHITEHOUSE. Yes, sir.

Chairman ENZI. The sources of the budget dysfunction are not new. Both parties are guilty of adding additional uncertainty, so it is ripe for abuse. And the process is not a substitute for good policy, but a functional process would be a constructive venue for us to start with. And I am pleased that we have these witnesses today to help us a little further along down the road.

We have Dr. Kevin Hassett, who is the director of economic policy studies at the American Enterprise Institute. He is a senior economist on the Board of Governors of the Federal Reserve System and an associate professor of economics and finance at Columbia University Business School. He also served as a policy consultant to the U.S. Department of the Treasury during the George H.W. Bush and the Bill Clinton administrations.

Dr. Philip Joyce is the senior associate dean and a professor of public policy at the University of Maryland School of Public Policy. He has 12 years of experience in public service, including 5 years at the Congressional Budget Office. In 2012, he published a report entitled, "The Costs of Budget Uncertainty."

Our third witness is Norman Ornstein, a resident scholar at the American Enterprise Institute. He is also a contributing editor and a columnist for National Journal and The Atlantic.

So I thank you for joining us today to share your expertise on this important subject, and, of course, at the conclusion of the day, those who are not here and those who are can also submit questions that we hope you will answer. I try to save some of my accounting questions for doing them in writing.

So thank you for being here. Dr. Hassett.

**STATEMENT OF KEVIN A. HASSETT, PH.D., DIRECTOR OF ECONOMIC POLICY STUDIES, AMERICAN ENTERPRISE INSTITUTE**

Mr. HASSETT. Thank you, Mr. Chairman and Senator Whitehouse and other members of the Committee. It is really an honor to be back here.

I have been working on one aspect of this problem for most of my career, and the focus of much of my academic research has been trying to quantify policy uncertainty and then investigate what the impact of policy uncertainty might be. My testimony, which, as I am wont to do, often is much longer than I could possibly discuss in 5 minutes, and so I will summarize the main points briefly.

I think that there has been an explosion recently in academic work that has found that policy uncertainty is a big negative for the economy, and in my testimony, I discuss some of the evidence and also try to make it intuitively appealing so that folks can understand why it happens.

Uncertainty can basically go up in any setting if the odds of different things happening move towards 50/50. So if it is a 100-percent chance that something is going to happen, it is not that uncertain; if it moves towards 50/50, then it can be very uncertain.

Uncertainty can go up if the set of things that might happen get farther and farther apart, so imagine if, you know, one party wins, then the tax rate is going to be really high; if another party wins, the tax rate is going to be really low. And the disagreement about the tax rate goes up over time so that the tax rates that might happen if there is an election get farther and farther apart.

Those are the kind of things that can drive up uncertainty, and if you watch the political climate in the U.S. and how it has evolved over the 17 years that I have been at AEI and a colleague of Norm's, then one of the things that we have seen is that the parties have gone pretty efficiently towards having a 50/50 chance of winning quite often. And it seems to me that often their policy positions have grown farther apart. And so that the impact of policy uncertainty is something that one should really take seriously.

In the literature, we find that the heightened policy uncertainty that we see is a big, identifiable negative effect on the economy, and on page 4 in my testimony, if you have it with you—otherwise, I could just walk through it—I show some of the evidence from the literature where some University of Chicago and Stanford economists have developed a measure of uncertainty. In my chart, I show how the policy uncertainty evolves over the political cycle. It tends to peak in a Presidential election year—go figure—and has a really big statistically significant negative effect on risk spreads. And so if you are a somewhat risky borrower, then it costs you a lot more to borrow money, and equity prices tend to go down with policy uncertainty is high as well.

That chart actually helps you understand what policy uncertainty does, how it affects the economy, because suppose that you wanted to borrow money to do something at a time when spreads are wider, well, then, it is going to cost you more, so you might do less of it. But there is another factor in the literature that is equally or maybe more important, and that is that when there is a lot

of uncertainty, then people who maybe are deciding to buy a car or build a factory tend to want to wait and see. And so if you are thinking about whether you are going to expand your business right now, you might really be worried about doing it until you see what happens in November. And so you could see capital spending dropping a lot when political uncertainty is high.

That is kind of where the effects come through, and I talk about that in my testimony. And in the end of that section, I also talk about the fiscal cliffs and debt limits. We have got a little bit of evidence on those and show that the risk spread effect that we see over the Presidential election cycle is actually a little bit magnified near big budget showdowns.

And so this policy uncertainty is something that you could have an effect on. If we knew that policy was going to be pretty much set going forward and that there were not going to be fiscal cliff showdowns, then risk spreads would go down. There would be more investment. And it would be less likely that somebody might wait to get across a threshold in order to do their investment.

But if we are in this world where we are having a fiscal cliff every other year and policy might swing willy nilly, depending on what happens at the election, then you are going to see a lot of waiting to see what happens in the next election. And so almost every other year, economic activity could be very much suppressed because of policy uncertainty.

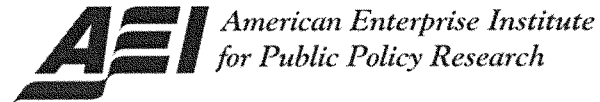
In the last part of my testimony, I talk about long-run policy uncertainty, and, again, this circles back to, Mr. Chairman, your main point here, which is, What could we do to address policy uncertainty both in the short and the long run? And there is a lot of evidence that if you have a fiscal consolidation—so that right now we all know that looking out 40 or 50 years that we are not really looking at sustainable fiscal policies. If you have a fiscal consolidation, something that makes long-run policy sustainable, then you reduce a lot of long-run uncertainty. Right now you are probably not rushing out to invest in a new factory in Greece because you do not know how that government is going to work it out. We are not Greece yet. But if you look off into the future, then maybe people will start to think about it that way, too.

The evidence is that if you fix long-run situations, then you do not necessarily have the negative effect you might expect from tax increases and spending cuts, and I think that the main reason that probably happens is that uncertainty, the reduced uncertainty, offsets those effects.

And so near-term uncertainty tends to be something that is related to fiscal cliffs. Long-term uncertainty is something that is related to big, unsustainable shortfalls. I think that if this Committee could take the lead in addressing both, the economic benefits could be significant.

Thank you.

[The prepared statement of Mr. Hassett follows:]



Statement before the Senate Budget Committee  
*Fixing Broken Budget Process and Restoring Stability to Government Operations*

Kevin A. Hassett  
Director of Economic Policy Studies and State Farm James Q. Wilson Chair  
American Enterprise Institute

April 20, 2016

*The views expressed in this testimony are those of the author alone and do not necessarily represent those of the American Enterprise Institute.*

Chairman Enzi, and Members of the Committee, I thank you for inviting me to talk about the negative effects of uncertainty and dysfunction in the budget process. In my testimony, I will discuss the latest economic research investigating the impact of uncertainty on the overall economy, and relate uncertainty about the budget to this literature.

Few topics in Washington engender consensus among economists from both sides of the political spectrum. The existence of negative effects of budget uncertainty and dysfunction, however, seems likely to be one of them.

Uncertainty is, of course, with us every day. We don't know if it will rain tomorrow, or if a drought might begin that would cause severe harm to crops. A car manufacturer might wake up one day and find that Tesla has invented something new that fundamentally affects the demand for internal combustion engines. When uncertainty is higher, then economic agents become more cautious. If, for example, a manufacturer in a rapidly evolving industry came to you for a loan, you might be wary of making it, and charge a higher interest rate if you do.

There are many types of uncertainty that we cannot have much of an impact on, but there are some that are under the control of policymakers. If our citizens believe that tax and spending policies are unpredictable, then they will act as if the world is more uncertain, and be wary of making purchases and investments that they might otherwise make.

As we think about policy, there are two ways we should think about uncertainty increasing. First, suppose that we have a two party system, and the two parties have different views about the best level for the corporate tax rate. If one party is sure to have power, then there is not much uncertainty. Its desired rate will likely prevail. But if the odds of either party controlling the government move towards a true 50-50, then we can say that uncertainty has increased relative to a world the odds were, say, 70-30. Second, if the beliefs of the two parties concerning the best tax rate grow farther apart, with one party favoring much lower rates, while another favors much higher rates, then the widening of the spread between things that might happen is another form of increased uncertainty.

If we have become more evenly divided politically, and at the same time, the policy views of the parties have grown farther apart, then we can say with a great deal of confidence that the political situation has evolved in a way that could increase the harmful effects of economic uncertainty.

This is not just an abstract theoretical observation. As I will discuss in my testimony below, there has been an explosion of research that has suggested that the negative effects of policy uncertainty may be quite large indeed. In what follows, I will divide my testimony into an analysis of two types of uncertainty that policymakers should consider when designing optimal policies. Short-term uncertainty in a budgetary context concerns uncertainty likely to arise from events that happen at predictably shorter time horizons, like spending authorizations or the "fiscal cliff" of 2011, or even elections. Long-term uncertainty, by contrast, concerns the trajectory of events that occur over lengthier horizons. An example of such long-term uncertainty would be uncertainty about the fiscal trajectory of the United States more broadly, or, to take a concrete example, the solvency of the Social Security program.

Both of these types of uncertainty, distinct in theory, but interrelated in practice, are germane to the United States. On the long-run front, the CBO's March 2016 baseline project projections forecast that the deficit as a share of GDP will have increased by more than 60% over its 2015 level by 2026, and in the years that follow, deficits will remain on a trajectory that quite quickly could make the United States see a fiscal situation as bad as that of Greece today. When a path is unsustainable, policies must change. Uncertainty about how they might change is a major factor for decision makers. And on the short-run front, Congressional bottlenecks like the 2011 fiscal cliff seem almost as much a part of Washington as the cherry blossoms. As importantly, the wide disagreements between the parties about policy, and the potential for wild swings in key fundamentals around elections have clearly had a big impact on markets.

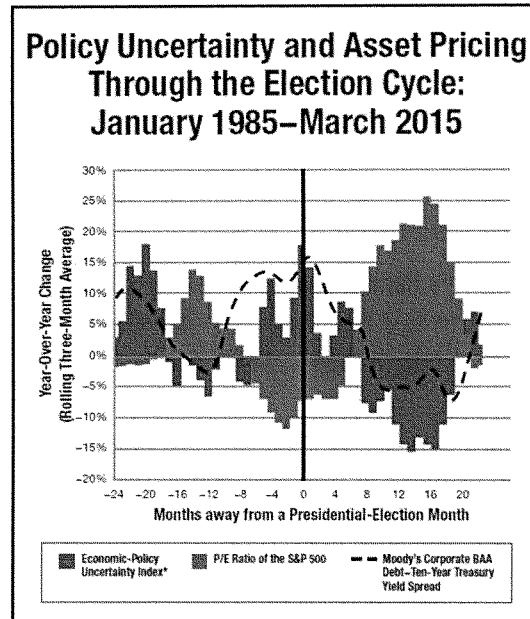
### **Short-term uncertainty and its negative effects**

There now exists a large and still growing academic literature on the effects of uncertainty. Economists disagree about how to quantify uncertainty, how to best identify its effects, and on their magnitude. But they have developed a number of innovative measures, and found that uncertainty has a major impact on the economy.

Perhaps the best-known recent work on uncertainty has been performed by two economists at Stanford along with their colleague at the University of Chicago.<sup>1</sup> Baker, Bloom and Davis (2016) construct a measure of the uncertainty about policy by scraping through web sites and news stories to track the frequency with which observers mention the possibility of policy changes. They employ sophisticated econometric techniques to identify the link between uncertainty and economic activity, finding that the link is a powerful one. For example, they find that policy uncertainty around the Great Recession likely accounted for about an extra 1 percent drop in production. The harmful impact of policy uncertainty can be seen even without the sophisticated econometrics. The chart below, which draws from a paper my coauthor and AEI colleague Joseph Sullivan and I presented at a conference last year, plots both an index of economic policy uncertainty developed by Baker, Bloom and Davis, along with a measure of credit spreads and a measure of equity valuations throughout the four-year presidential election cycle. To make the data easy to interpret we changed the time scale over this sample period to "election time." Time zero is the November of a presidential election year, Time -1 is the October before said election, and time -24 is the midterm election.

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<sup>1</sup> This work is summarized and updated at: <http://www.policyuncertainty.com/>, a website that hosts the index created by Scott Baker of Northwestern University's Kellogg School of Business (and who was a graduate student at Stanford when the index was first created), Nicholas Bloom of Stanford, and Steve Davis of the University of Chicago Booth School of Business, and links to a number of academic works that explore the impact of uncertainty on the overall economy.



The equity valuation metric, the price-to-earnings ratio of the S&P 500, measures the price a firm can charge an investor in exchange for the claim on the firm's earnings that a share of its stock represents. A relatively high P/E ratio serves as an indication that the firm can raise capital at a relatively low cost: When the P/E is higher, it means the market perceives the equity to be less risky. The spread between the yield on Moody's BAA-rated debt and the ten-year Treasury yield is an alternative measure of the risk premium. It indicates how much market participants demand in exchange for holding bonds that, according to Moody's, come with "moderate credit risk" and have "certain speculative characteristics." A larger spread indicates that market participants are charging businesses more for buying their bonds instead of the "risk-free" bonds of the U.S. government.

As the chart shows, stock valuations and debt spreads both respond adversely to the increases in uncertainty that seem to come with the election cycle. The effects are large. So the fact that the parties have grown so far apart, adds significantly to uncertainty, raising the cost of funds for

investors and consumers. This higher cost of funds reduces economic activity, which may explain some of the large impact on jobs and growth found in the literature.<sup>2</sup>

The broader literature has documented similar effects in many different corners of financial markets. For example, public security markets exhibit higher volatility in close proximity to U.S. elections. Li and Born (2006) find that U.S. equity markets become more volatile as presidential elections approach.<sup>3</sup> In a pivot to the state level, Gao and Qi (2012) find that municipal bonds floated by state governments immediately before an election pay a premium of six to eight basis points due to this electoral proximity.<sup>4</sup> Jens (2013) estimates that gubernatorial elections reduce state-level investment by between 5% and 15%.<sup>5</sup> Finally, Julio and Yook (2013) find that flows of cross-border foreign direct investment but not portfolio flows are sensitive to proximity to the timing of foreign elections.<sup>6</sup>

Think about it this way. Suppose you were running a firm, and you were contemplating making a billion dollar investment in a new factory. As we look ahead toward this November, there is no question that there is a great deal of uncertainty concerning who might win, and what policy might look like depending on the victor. Given the wild swings in policy that are conceivable, one could easily imagine that you might decide to postpone making that investment until after you see the election results. The data suggest that these effects are very important for understanding the evolution of the economy, and in all likelihood, the weakness of the economy today.

It would not, of course, be advisable to seek to reduce uncertainty by eliminating elections. But if the Senate, in particular, could move more toward a policy consensus based on science and evidence, then markets would worry less that policy would change course on a dime at each presidential election. The reduction in uncertainty would likely, given the literature, have significant positive economic benefits.

The same authors have recently created indices that focus specifically on the prospects of a government shutdown or a failure to raise the debt ceiling. As with the broader uncertainty index, the chart measures uncertainty about the debt ceiling or a government shutdown by counting the fraction of articles in major newspapers that have language on the subject. The chart below plots how these metrics have changed through time. The events that one would expect to

<sup>2</sup> See <https://bfi.uchicago.edu/sites/default/files/research/hassett-sullivan.pdf> for more on the literature and this chart.

<sup>3</sup> Li, Jinliang, and Jeffery A. Born. 2006. "Presidential election uncertainty and common stock returns in the United States." *Journal of Financial Research* 29 (4): 609-622.

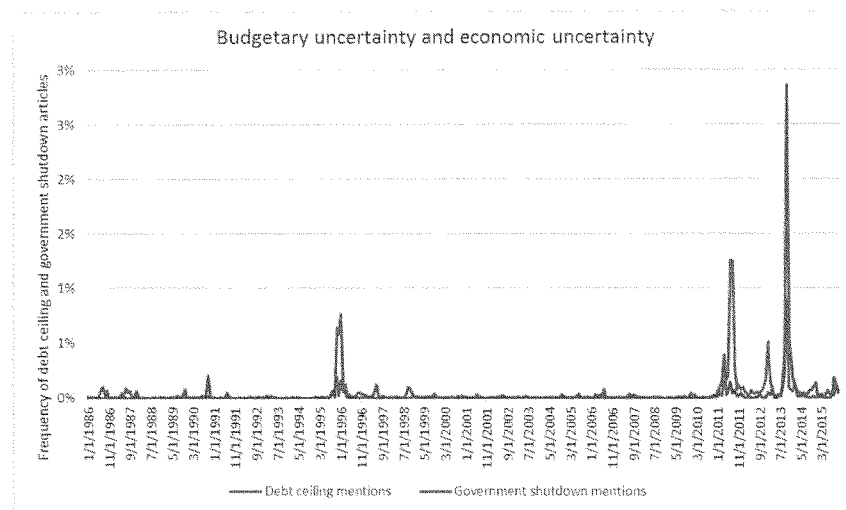
<sup>4</sup> Gao, Pengjie, and Yaxuan Qi. 2012. "Political uncertainty and public financing costs: Evidence from US municipal bond markets." [http://extranet.isnie.org/uploads/isnie2012/qi\\_gao.pdf](http://extranet.isnie.org/uploads/isnie2012/qi_gao.pdf)

<sup>5</sup> Jens, Candace. 2013. "Political uncertainty and investment: Causal evidence from US gubernatorial elections." [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2176855](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2176855)

<sup>6</sup> Julio, Brandon, and Youngsuk Yook. 2013. "Policy Uncertainty, Irreversibility, and Cross-Border Flows of Capital." [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2024612](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2024612)



observe—the 1995 government shutdown, the 2011 flirtation with the debt ceiling, and the 2013 fiscal cliff—are all visible on the chart.



Interestingly, my own analysis performed while preparing this testimony finds that these spikes in uncertainty have negative effects that are quite similar in magnitude to those already linked to policy uncertainty more generally. To link this to presidential uncertainty, we estimated the average values of our measure of credit spreads and our measure of equity valuations when either the debt ceiling or government shutdown series were more than two standard deviations above their average values. When debt ceiling uncertainty rose two-standard deviations or more above its average, the S&P 500 P/E ratios were 28.9% lower than in normal periods and credit spreads were 8.75% higher.<sup>7</sup>

#### Longer Term Uncertainty and Fiscal Consolidation

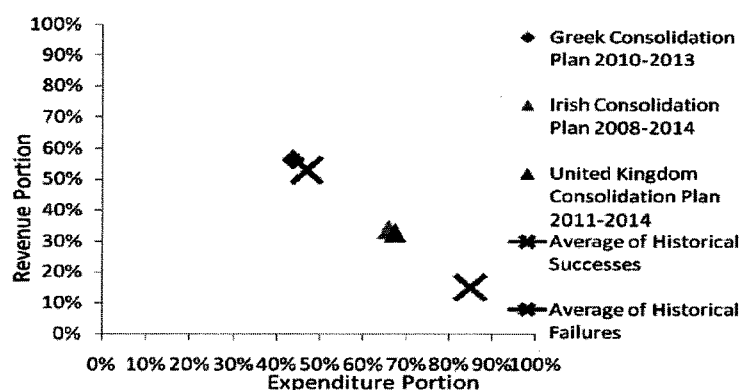
Uncertainty surrounding the budget stems, at least in part, from the unsustainable deficits that the government seems to run year-after-year. If the U.S. exhibited at least some capacity to make the combination of spending and tax adjustments necessary to eliminate or even reduce its deficit, uncertainty about the long-term fiscal trajectory of the United States would be diminished. In such a world, after all, budget fights would be less complex and consequential: if tax revenue funded government spending, merely keeping existing policy in place would suffice. The

<sup>7</sup> The sample for this estimate runs from January 1986 to November 2015.

interconnected web of spending authorizations and expiring tax cuts that beguiled legislative attempts at resolving the fiscal cliff would no longer make their regular appearance.

Other countries have undergone fiscal consolidation in the past, providing us examples of policies that are successful and as well as examples of those that have failed. Along with two colleagues, I have written an analysis<sup>8</sup> exploring policy mixes in successful and failed fiscal consolidations in 21 OECD countries, with the measure of success simply being that the consolidation accomplishes the objective of stabilizing the debt. We found that fiscal consolidations based more heavily on expenditure cuts than revenue increases are more likely to be successful at producing lasting reductions in debt.

Using a range of different methodologies, we find that the average unsuccessful fiscal consolidation relied upon 53 percent tax increases and 47 percent spending cuts, while a typical successful consolidation consisted of 85 percent expenditure cuts. We also found that cuts to social transfers were more likely to reduce deficits than other expenditure cuts. The chart below shows the composition of average successful and unsuccessful consolidation plans, along with a few measures taken recently by other countries.



Other research has reported similar findings, most notably an earlier paper by Alesina and Perotti<sup>9</sup>, which found that consolidations successful in reducing debt consisted of 64 percent spending cuts and 36 percent tax increases. Similarly, McDermott and Wescott found in a survey

<sup>8</sup> Andrew G. Biggs, Kevin A. Hassett, and Matthew Jensen, "A Guide for Deficit Reduction in the United States Based on Historical Consolidations That Worked," AEI Economic Policy Working Paper 2010-04 (2010) <http://www.aei.org/paper/100179>.

<sup>9</sup> Alberto Alesina and Roberto Perotti, "Fiscal Adjustments in OECD Countries: Composition and Macroeconomic Effects," *NBER Working Paper* 5730 (1996)

of fiscal consolidations that expenditure-based consolidations had a 41 percent chance of success, while revenue-based consolidations have only a 16 percent success rate.<sup>10</sup>

Normally, tax increases and spending cuts might be expected to have near-term negative effects on the overall economy. The tendency of successful fiscal consolidation to at times even have positive short term growth effects likely reflects the positive effects on sentiment, consumer spending and investment that accompany reduced uncertainty. Such positive effects are quite intuitive. For example, one might not have a great deal of confidence in an investment in Greece precisely now. Your successful factory might well be served by a rotting infrastructure poorly supported by a bankrupt government, and still be taxed with abandon in the future. But if Greece could restore fiscal sanity, an investment might be a good deal more attractive. That's why consolidations can lead to positive economic developments.

#### **Looking ahead: entitlement reform**

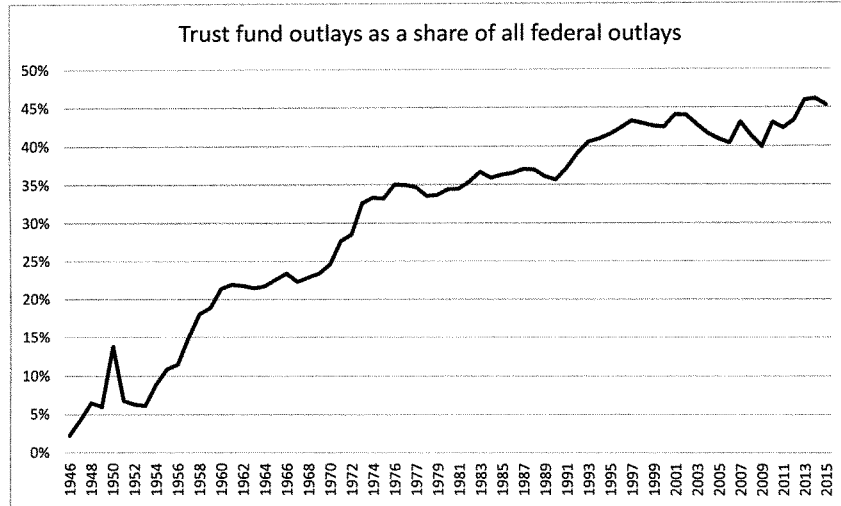
The data suggest that the U.S. is overdue for a fiscal consolidation.

The "trust fund" share of federal outlays—the share attributable to Social Security or Medicaid funds—has steadily risen since World War II. In 1946, these were only 2.2% of federal outlays. By 2015, however, they have become no less than 45.3% of federal outlays, according to data from the Office of Management and Budget.<sup>11</sup>

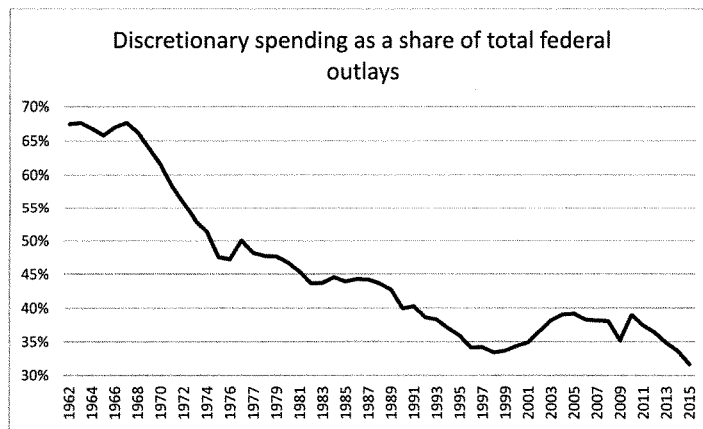
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<sup>10</sup> McDermott, C. John and Wescott, Robert, An Empirical Analysis of Fiscal Adjustments (June 1996). IMF Working Paper, Vol. pp. 1-26, 1996. Available at SSRN: <http://ssrn.com/abstract=882959>

<sup>11</sup> The data come from Table 1.4: Receipts, Outlays, and Surpluses or Deficits (-) by Fund Group: 1934-2021, available at: <https://www.whitehouse.gov/omb/budget/Historicals>.



Perhaps as a consequence, then, the share of federal outlays attributable to discretionary spending has also fallen considerably. Though discretionary spending constituted 67.4% of outlays in 1962, today that number has fallen to 31.6%, according to the Office of Management and Budget.<sup>12</sup>



<sup>12</sup> The data come from Table 8.7: Outlays for Discretionary Programs: 1962-2021, available at: <https://www.whitehouse.gov/omb/budget/Historicals>

Neither of these trends seem sustainable: just as it is difficult to imagine trust fund spending as a share of the federal budget continuing to increase in the 21<sup>st</sup> century in the same way that it increased during the second half of the 20<sup>th</sup> century, it is difficult to imagine discretionary spending continuing to shrink as a share of the federal budget at the same rate as it has over the last half of the 20<sup>th</sup> century during the 21<sup>st</sup> century.

It is clear, then, that the situation of America's entitlement programs generates substantial long-run uncertainty. Either we will face solvency issues or policymakers will need to undertake bold and politically difficult entitlement reform.

Clearly, Ben Franklin's famous saying should be modified. Today, nothing can be said to be certain except death, taxes, and uncertainty. The latest economic literature suggests that this uncertainty is harmful in both the long and short runs, and that the benefits of policies to address it could be significant.

Chairman ENZI. Thank you.  
Dr. Joyce.

**STATEMENT OF PHILIP G. JOYCE, PH.D., PROFESSOR OF PUBLIC POLICY AND SENIOR ASSOCIATE DEAN, UNIVERSITY OF MARYLAND SCHOOL OF PUBLIC POLICY**

Mr. JOYCE. Thank you, Mr. Chairman, Senator Whitehouse, members of the Committee. I first want to congratulate the Committee for deciding to highlight the subject of the apparently invisible, yet insidious, effects that budget uncertainty creates for both Federal agencies and recipients of Government funds. My comments are going to be informed by 25 years of participating in and watching the budget process, but also, as you noted, Mr. Chairman, a report that I wrote in 2012 for the IBM Center on the Business of Government. I also would recommend to you some work that was done by GAO in 2009 which also documents some of these effects.

You have already done a very good job of talking about the failings of the current budget process, so I will not talk about that. But I will say that my main point is that Government shutdowns get all the press, but Government by continuing resolution is perhaps more harmful because it is more routine.

Budgeting is about planning for the future. Any organization, whether it is the Federal Government, State and local government, or business, needs to have some notion of the funds that it will have available and when those funds will be available in order to effectively manage.

My testimony talks about some negative effects on people who get money from the Federal Government, but in my oral statement, I would like to focus on some of the main consequences for Federal management and for the cost of providing services.

First, budget uncertainty disrupts service delivery. Agencies engage in hiring freezes. That robs high-priority programs of staff because employee turnover does not occur equally throughout an agency. Further, there are often furloughs. Furloughs lower morale. Lower morale encourages employees who have other options, who are the ones that we least want to lose, to leave Government, which robs us of some of our best employees.

Second, CRs freeze priorities in place. Agencies have difficulty responding to new threats and problems and are required to keep funding outdated or ineffective programs.

Third, CRs may require governments to engage in short-term contracting as agencies have to often squeeze 12 months of contracting work into perhaps less than half a year. Moreover, it is widely believed that many contractors dealing with the Federal Government include what I would call a "risk premium" in the rate that they charge for contractual services because they cannot negotiate reliable multi-year commitments without some fear of funding interruption.

Fourth, agencies spend a lot of time preparing for potential Government shutdowns and CRs and then complying with them after the fact. In my view, this is a complete waste of time.

Finally, agencies defer investments in either people or physical assets, which I think compromises their effectiveness and leads to

higher future costs. For example, there have been in the past measurable reductions in training in the Department of Defense because they are operating under CRs and do not know how much money they are going to have or when they are going to have it.

What to do then? I would first say that many of the same people who decry waste in Government are themselves contributing to that waste by failing to provide a predictable funding stream for Federal agencies and recipients of Federal funds. When State and local governments have funding delays—and we do not have to look any further than the States of Illinois and Pennsylvania right now, which went most of this fiscal year without a budget—it results in lower bond ratings, increased borrowing costs, and likely political fallout. There is no evidence that these market signals work in the case of the Federal budget process.

The obvious point then is that the best thing that could be done would be to enact appropriations on time. That seems particularly unhelpful to stop there, so I have a few recommendations of things that might be done if we have to live with continuing resolutions.

First, I think the Congress should give agencies more flexibility in spending. The first way to do this would be by increasing the percentage of money that is available on a multi-year or no-year basis, which would especially assist those agencies with lots of grant and contract funding. I also think the requirements imposed on some agencies to have spending plans approved by congressional committees are a costly luxury when appropriations are 3 or 6 months late.

Second, I would make it harder to pass continuing resolutions than it is to pass regular appropriations bills. This may seem like an odd recommendation as it increases the probability, at least theoretically, of a Government shutdown. My point is that perhaps if there was more urgency in enacting appropriations, it would increase the odds of them being enacted sooner. And as I suggested earlier, Government by continuing resolution routinely might be worse than a Government shutdown.

Third, if we are to have CRs, I think they should be limited to only one or two per year that do not extend past the end of the calendar year. All CRs are not created equal. It matters how many there are, and it matters how long agencies have to operate under them. Problems created by multiple CRs—and there have been as many as 21 in a single year—or CRs last 4 months or 6 months are well documented.

So in the end, funding delays have costs. Those are financial costs and costs felt through compromised Government effectiveness. Either way, these are completely self-inflicted wounds, and I congratulate the Committee for thinking about what it is that we might be able to do to reduce their effects.

Thank you.

[The prepared statement of Mr. Joyce follows:]



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SCHOOL OF PUBLIC POLICY

Testimony of Philip G. Joyce  
Professor of Public Policy and Senior Associate Dean  
University of Maryland, School of Public Policy

Before the Committee on the Budget  
United States Senate

on

“Tap-dancing on the Razor’s Edge: Restoring Stability to Government Operations”

April 20, 2016



Chairman Enzi and members of the Committee:

Thank you for asking me to testify today on this important topic. I congratulate this committee for deciding to highlight the subject of the apparently invisible, yet insidious, effects that budget uncertainty creates for both federal agencies and the recipients of government funds. My comments today are informed by my own 30 years of observing the federal budget process, and some recent research that I have done culminating in a report written in 2012 for the IBM Center on the Business of Government.<sup>1</sup>

No one paying even casual attention to the routine dysfunction of the federal budget process in recent years—from “fiscal cliffs” to sequestration to government shutdowns and threats of shutdowns—could avoid coming away with the impression that the federal budget process is not working well. It would be somewhat reassuring to think that this recent experience was exceptional, and that we could now return to normal. Unfortunately, however, it is just the latest example of a system where we limp along from one crisis and missed deadline to another.

While actual government shutdowns are rare, “government by continuing resolution” is now the normal way of doing business, creating costs and problems of its own. The insidious effects of the chronic uncertainty that routine CRs create for federal agencies and recipients of government funds are at least as worthy of attention, and may indeed be more damaging, than the more high profile instances of sequestration or brief government shutdowns. Some of these costs are financial, and some represent inefficiencies and compromised effectiveness for federal programs. All of these negative impacts are self-inflicted, however, and are entirely preventable.

In my testimony today, I will do four things:

- Review the practice of late appropriations and other actions that create uncertainty in the federal budget process;
- Discuss the specific costs and effects of this dysfunction on federal agencies;
- Describe some of the effects of uncertainty that trickle down to recipients of government funds; and
- Offer suggestions as to how these costs and effects might be reduced in order to promote more efficiency and effectiveness in government programs and agencies.

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<sup>1</sup> Philip Joyce, *The Costs of Budget Uncertainty: Analyzing the Impact of Late Appropriations* (Washington: IBM Center for the Business of Government, 2012).

Shutdowns and Continuing Resolutions—Past Experience

The 1974 Congressional Budget and Impoundment Control Act, which created the modern congressional budget process, moved the start of the federal fiscal year from July 1 to October 1. This occurred in part to accommodate the additional steps created by the 1974 Budget Act, and in part because the Congress had a difficult time enacting appropriations prior to the start of the fiscal year. Ironically, however, the appropriations process has not gotten more timely since the 1974 Act. In fact, in only 4 of the 40 fiscal years since 1977 (the first year under the new process) have all appropriations bills been passed and signed into law prior to the start of the fiscal year.

In the first years following the advent of the new process, there were limited consequences of late appropriations, because agencies continued to operate normally even in the absence of funding. Agencies assumed that the Congress intended for them to continue operating, and that the required funding would be forthcoming. This changed in 1980 when Attorney General Benjamin Civiletti issued an opinion stating that agencies did not have legal authority to spend money in absence of appropriations. After the Civiletti opinion, continuing resolutions became the norm, since they were necessary (in the absence of appropriations) in order for agencies to continue to operate. Short funding gaps were relatively routine, but many of these occurred over holiday weekends and the impacts were not widely felt. Between fiscal year 1982 and fiscal year 1988, there were nine such funding gaps (sometimes two in a single year) but their average duration was two days. While technically these might have been government shutdowns, they had a very small impact.

The fiscal year 1996 budget process, however, yielded the longest government shutdowns in history, totaling 26 days. The first lasted from November 14<sup>th</sup> to November 19<sup>th</sup>, 1995, and resulted in the furlough of 800,000 federal employees in agencies covered by appropriation bills that had not been enacted. A second, much longer, shutdown commenced on December 16<sup>th</sup>, 1995, and lasted for three weeks—until January 6, 1996. This second shutdown only furloughed 284,000 federal employees; the number was reduced mainly because several more appropriation bills had been enacted in the interim.

While a thorough discussion of this shutdown is beyond the scope of this hearing, later studies estimated a financial cost of \$1.4 billion (mostly resulting from paying employees retroactively for work that was not done), in addition to substantial negative effects on service delivery. For example, almost 400 National Park Service facilities were closed, affecting 7 million visitors. Further, the Social Security Administration did not process about 200,000 applications for benefits, and 800,000 toll-free calls went unanswered. More recently, the fiscal year 2014 budget process resulted in a government shutdown that

commenced on the first day of the fiscal year (October 1, 2013), and lasted for 16 days. An analysis by the Office of Management and Budget estimated a number of costs associated with this shutdown. They included a loss of \$2 billion to \$6 billion in domestic economic output, and another \$2 billion in costs associated with paying federal employees retroactively for work that was not done.<sup>2</sup>

While there were no shutdowns between the fiscal year 1996 shutdown and the one affecting fiscal year 2014, and no shutdowns for fiscal year 2015 or fiscal year 2016, this does not mean that the appropriations process has operated smoothly in the absence of a shutdown. In fact, we have experienced government by continuing resolution every year since 1997; increasingly there have been more of these per year, and they have extended further in to the fiscal year. For the 19 fiscal years between 1998 and 2016, there were an average of almost 6 CRs per year (the high point was fiscal year 2001, when there were 21) and CRs, on average, covered an average of 3 months (excluding the three years—2007, 2011, and 2013—in which there were full-year CRs).<sup>3</sup>

#### Effects of Budget Uncertainty and Crisis Budgeting on Federal Agencies

The failure to enact timely appropriations creates an environment of substantial uncertainty for federal agencies and for recipients of federal funds. The focus—by the public and the news media—tends not to be on this routine dysfunction and the problems that it creates, but on the immediate crisis: How do we avoid going over the fiscal “cliff”? How do we avoid a government shutdown? How do we prevent a debt default? The effects of funding delays caused by routine CRs, however, are significant.

Budgeting is about planning for the future. Any organization—whether it is the federal government, a state or local government, or a business—needs to have some notion of the funds that it will have available in order to effectively budget, and manage. The more certainty that exists, the better informed the decisions are, and the more effective the result. For the federal government, late appropriations and “government by CR” have created a number of specific problems:

- CRs have various effects on government personnel, including hiring freezes that create skill gaps in crucial areas, and morale and turnover problems, often as a direct result of employees feeling as if they are pawns in a larger political game over which they have no control.

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<sup>2</sup> Clinton Brass, *Shutdown of the Federal Government: Causes, Processes, and Effects*, Congressional Research Service, September 8, 2014.

<sup>3</sup> James Saturno and Jessica Tollestrup, *Continuing Resolutions: Overview of Components and Current Practices*, Congressional Research Service, January 16, 2016.

- Because CRs require the continuation of current activities, agencies have trouble responding to many new problems and are required to keep funding outdated or ineffective programs.
- CRs may require agencies to engage in short-term contracting, which significantly increases contracting workload and overhead costs. In addition, delays in contracting can lead to higher costs for individual contracts and also higher costs resulting from less competition.
- Investments that are not made—in people (as training is cancelled or deferred) or infrastructure (in the form of deferred maintenance) lead to higher future costs.
- Agencies waste a great deal of time preparing for potential government shutdowns and CRs, and then complying with them after the fact.

Delayed Hiring and Personnel Actions, and Morale Issues. Because personnel costs are such a substantial portion of many agency budgets, managing delays in funding necessitates reducing personnel spending. This often leads to hiring freezes or across-the-board cuts. Hiring freezes can create skill gaps in parts of the agency where turnover is greatest. This means that a hiring freeze can end up robbing the agency of personnel working in higher priority programs, or can have an unintentional differential effect if vacancies are concentrated in particular programs, projects, or activities.

In cases where funding delays lead to concerns that a shutdown or sudden budget reduction may follow (as occurred in 2011 and 2013) agencies may be required to prepare furlough plans and to send out furlough notices to employees. This can have unintended consequences, even in cases where the furloughs are unlikely to actually take effect. Some employees may respond to furlough notices by spending otherwise productive time seeking other employment. Those who end up leaving (because of fear of furlough, or because they are just fed up) are likely to be those who were just hired or who have other options. In either case, they are not necessarily the ones that an agency would choose to terminate if the agency was focused on performance considerations.

Freezing Priorities in Place. Continuing resolutions also create problems in cases where agencies are attempting to shift priorities to respond to some immediate challenge facing them. If an agency has identified a need to shift personnel from one area to another, to address some area of immediate concern, this can delay its ability to respond. This is complicated further by the sheer amount of time that it can take to fill a position. A position that is approved in February or March might not be filled until August or September.

A 2009 GAO report on the effect of CRs cited numerous examples of this behavior.<sup>4</sup> For example, the Federal Bureau of Investigation (FBI) delayed filling existing positions in order to fund annual pay raises, annualize pay for previous year's hiring, or to cover increased costs of retirement, health insurance, or other employee benefits. GAO found other examples where hiring delays affected the number of FDA food inspections, the ability to maintain or improve the ratio of corrections officers to inmates, and the ability to process claims for veterans' benefits.

The fiscal year 2011 budget delays, leading up to a final agreement that was not reached until April 2011, is illustrative of the compromises to government effectiveness that can occur. Media reports indicated that DOD needed to raid procurement budgets in the first half of the year in order to fund pay and benefits, resulting in deployed troops not getting needed equipment, the cancellation of 20 ship overhauls by the Navy, and deferred aircraft maintenance. There were nondefense effects as well. In State College, Pennsylvania, a newly built \$7.5 million air traffic control tower, sat empty in the spring of 2011 because the Federal Aviation Administration lacked the funding to hire the air traffic controllers to staff it.

In addition to preventing new starts, CRs typically require activities that are ongoing to be continued. In other words, in addition to prohibiting agencies from doing NEW things, CRs also prohibit them from ceasing funding for OLD things. In one case the Department of Justice had decided to stop funding the National Drug Intelligence Center in Johnstown, Pennsylvania. Since they could not plan for a specific date to cease operations, the passage of a CR required them to continue operating until the regular appropriation became law.

Changes in Contracting Practices. Because late appropriations have become the "new normal" for agencies, they have adjusted their spending patterns to accommodate. The agencies interviewed by GAO in 2009 each reported that they delayed contracts. The Veterans Health Administration (VHA) said that they did not start nonrecurring maintenance projects, but instead waited until the regular appropriation was received. Delays can also lead to a rush to obligate at the end of the year. VHA reported to GAO, for example, that in 2006 they obligated 60 percent (about \$248 million) of a \$424 million nonrecurring maintenance budget in September, the last month of the fiscal year. This rush creates a greater potential to make mistakes, which may lead to wasted funds and adverse audit findings.

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<sup>4</sup>Government Accountability Office (2009). *Continuing Resolutions: Uncertainty Limited Management Options and Increased Workload in Selected Agencies*, September.

In addition to delaying contracts, many agencies also are forced to enter into multiple contracts for a much shorter time period (instead of one yearly contract), so that the duration of the contract can more-or-less match the duration of the CR. For example, BOP awarded a contract in 1997 to an optometrist to provide care for a prison. Under a regular appropriation, this would have been a one-year contract. Instead, there were three contracts covering only the first quarter of the year: 1) October 1 to November 16; 2) November 19 to December 14; and 3) December 17 to December 21. This kind of short-term contracting creates substantial additional workload—more contracts means more work, higher administrative costs, and greater opportunity for errors and waste.

These changes in contracting practices often lead to increases in costs. The Bureau of Prisons (BOP) reported to GAO that a CR lasting longer than 3 to 4 months typically negatively affects the quality of competition. In addition, delayed contracts may have higher prices. BOP said that awarding contracts later prevented the agency from locking in prices and therefore increased costs. In one case (the McDowell Prison facility in West Virginia), this resulted in about \$5.4 million in additional costs. The precision of this estimate is exceptional; most agencies know that costs are higher, but are unable to confirm specific dollar amounts of increased costs.

Along these same lines, it seems quite likely that many contractors dealing with the federal government include a “risk premium” in the rate that they charge for contractual services, because they cannot negotiate reliable multi-year commitments without fear of funding interruption. Federal agencies pay more for services than an equivalent private firm would pay for the same service. While the existence of such a premium is widely assumed, it is difficult, if not impossible, to estimate it with any precision.

Failing to Invest in Training, Travel and Maintenance. Travel and training, as areas where agencies typically have discretion to delay funding, are frequent candidates for cutbacks. One agency representative reported that the agency simply avoided sending staff to training in the first quarter of the calendar year. The later that the final appropriation is received, the more that training budgets (and therefore training) is likely to be reduced. In DOD, for example, training and the agency’s key challenge of maintaining force readiness are inexorably related. The various forms of budget uncertainty (the threatened government shutdown, and the debt ceiling impasse) led, in some years, to measurable reductions in DOD training. The Air Force, for example, predicted that CRs and planning for a shutdown in 2011 reduced flying hours by ten percent, and other active duty personnel interviewed in 2011 reported that the near shutdown led to the cancellation of training exercises.

Foregone maintenance also increases costs. There is little question that failing to properly maintain any asset reduces its useful life. This can have two possible impacts. It could simply take the asset in question out of service, thus depriving citizens of the benefits that would otherwise be received. Perhaps more likely, it will lead to future costs as the asset wears out more quickly. A very clear example of this potential comes from the 2011 funding delay, when the Navy cancelled seven ship-repair contracts, at a savings of \$62 million (McCabe, 2011). Even if these repairs occurred in a later fiscal year, their deferral could clearly have operational and cost implications.

Wasted Time and Effort, Leading to Reduced Effectiveness and Efficiency. Aside from increasing costs, continuing resolutions and funding delays invariably created additional work and cause agencies to take actions that compromise their efficiency and effectiveness.

A good place to start here is with the process of preparing for shutdowns, and for living with CRs. Staff in federal agencies, OMB, and the Congress spend a non-trivial amount of time preparing for things that usually do not happen (in the case of shutdowns) or which do happen, but which waste a lot of time in trying to lessen counterproductive or even illegal effects (in the case of a CR). In recent years in which there have been threats of shutdowns (especially in 2011 and 2013), OMB asked agencies to prepare shutdown plans. When this happens, both the OMB and federal agencies spent a great deal of time developing these plans and reviewing them, which is a complete waste of time unless the shutdown actually takes effect.

Preparing for CRs can also frequently be time consuming. One of the most time-intensive processes involves dealing with anomalies, which are specific exceptions to the general limitation on funding in CRs. Since, by definition, these anomalies are exceptions to the general rules governing a CR, many agencies invariably think that their peculiar circumstances deserve exceptional treatment. It is often quite difficult, however, to get the Congress to go along with anomalies. This leads to lots of negotiations between OMB and agencies over which things can and cannot be appropriately be included as anomalies.

These inefficiencies do not stop the moment that the CR is enacted. Agency budget offices, and OMB, are involved in lots of conversations around budget execution once the CR is law. Many of these discussions are designed to determine what can and cannot be done, and when something is a continuation of a current activity and when it represents something new. Agency budget officials often have to spend inordinate time responding to inquiries about what is and is not permitted under a CR. The

GAO case study agencies indicated that there were four types of administrative tasks most often affected by CRs:

- Issuing guidance to programs and offices;
- Providing information to Congress and OMB;
- Creating, disseminating and revising spending plans; and
- Responding to questions and requests for additional funding above the amount allotted.

There are no precise estimates of the costs of these tasks. GAO reported that VHA estimated that a one-month CR results in over \$1 million in lost productivity at VA medical facilities and over \$140,000 in additional costs for the VA contracting office.

Effects of CRs on State and Local Governments and the Private Sector.

The federal government provides substantial funds to state and local governments, in the form of grants, and to the private sector, in the form of contracts. The increased uncertainty, and the increasing length of time covered, by CRs has created increased costs and uncertainty for these sectors as well.

Federal grantmaking agencies reported to GAO, for example, that CRs that extended beyond about mid-February tended to delay discretionary grant announcements, thus pushing back both application reviews and awards. In some cases, grants were cancelled, even though the funds were eventually provided. A compressed application period can also decrease the quality of application and review, and discourage some potential recipients from applying for grants out of fear that they will have insufficient time to prepare grant applications, which can be complicated and time-consuming.

Agencies that award grants must decide, if operating on a long-term (more than three months but less than a full year) CR, whether to suspend grant application processes until an appropriation is received or to go ahead with them, pending a final appropriation. In the former case, there may not be enough time available for potential recipients to prepare applications and for agencies to process them in the second half of the year. Therefore, what appears to be a delay may result in a cancellation of the grant program, at least for the current year. In the latter case, there is a risk that, if the funds are not ultimately provided, the agency could have applications in hand but no funding for the program. This occurred in fiscal year 2011 with the Department of Education's Teaching American History program.



A similar story exists for contractors. When stories began to emerge in 2012 that speculated about the effects of sequestration, the first effects that were discussed were the impacts on federal contractors who had already started to react to the threat of across-the-board cuts. If contractors believe that an actual shutdown, or contract cancellation, is imminent, they face difficult questions concerning whether or not to continue work, and how long they can afford to keep employees on board. Whether late appropriations ultimately lead to layoffs depends on the contractor, and particularly on the rate of turnover. There certainly are cases, especially for small contractors, where layoffs are necessary. In 2011, for example, Penn State University's Applied Research Laboratory, heavily funded by a contract with the Navy, reported having to lay off 13 engineers due to funding reductions from the Navy associated with federal budget delays.

It is likely that the effects of uncertainty are felt more acutely by firms with the following characteristics:

- small businesses that may have less of a cushion against the delay in funding for an apparently small contract. Smaller businesses are less likely to have the capacity to “ride out the uncertainty” associated with funding delays;
- firms that work only for the government;
- firms that are funded from agencies that have primarily one-year money;
- firms funded by agencies that are more likely to receive late appropriations (some appropriation bills are more chronically late than others);
- contractors that are (especially within DOD) in the delivery stage of a given project (as opposed to development) because delivery involves higher personnel costs.

According to contractors who deal with both sectors, the biggest difference between commercial and federal work is that for commercial work the contractual firm can make long-term commitments, whereas with a federal agency the commitment is year to year. To the extent that there are capital costs, those capital costs can be captured with certainty over a three-to-five year period. A federal contract, conversely, may be a base contract with 10 one-year options.

In the end, it is true that, in general, government work tends to be more risky than commercial work. It is made even more risky in cases where there may be some interruption in funding as a result of a shutdown or default. A 2007 study, for example, of DOD contracting delays found that nine out of twelve companies included in the study experienced a decline in company stock values as a result of these

delays. It is likely that there are a significant number of contractors who are unwilling to work with the government, thus reducing competition and increasing costs.

#### What to Do About the Problem of Late Appropriations

Ultimately, the greatest impediment to fixing the problem of late appropriations is that their negative consequences seem to be largely invisible. Many of the same people who decry waste in government, however, may themselves be contributing to that waste by failing to provide a predictable funding stream to federal agencies and recipients of federal funds. No state or local government would be able to get away with this, without consequences, as chronic funding delays would result in lowered bond ratings, increased borrowing costs, and likely political fallout. Despite this, of course, both the states of Illinois and Pennsylvania have operated much of the current fiscal year without a budget. These cases are notable because of how unusual they are, and in both of these cases, the result has had the predicted result of higher bond ratings. These market signals do not seem to exist in the federal budget process.

Despite the apparent invisibility of these effects, however, it should be clear that routine timely appropriations would have many positive effects on budget formulation and execution, including the following.

1. If appropriations were timely, it would improve budget planning for future years. The clearest example of this has to do with the President's budget, where if the current year appropriations are not enacted by around mid-December, it makes it virtually impossible to have reliable information on which to base proposed funding for the budget year.
2. If decisions in budget execution did not have to be made in such compressed time frames, it would lead to better decisions since agencies would not be (at least to the same extent) rushing to make choices on contractors, grants, etc.
3. Agencies could begin to plan for hiring earlier in the year which (given how long it can take to fill a position) increases the chance that they will have a full complement available to deliver priority services.
4. Investments in employees and in physical assets would be able to be protected by permitting adequate funds to be provided for employee training and maintenance of this physical capital.
5. Both the cost of contractual services and their quality would be improved if appropriations were received in a timely manner. Predictability would enable agencies

to negotiate contracts at a lower price and contractors would likely deliver higher-quality service.

How can we encourage these positive effects? It is hard to avoid starting with the obvious conclusion: **Given all of the negative consequences of late appropriations, the Congress should discharge its most basic responsibility and routinely enact appropriations before the beginning of the fiscal year.** It is hard to imagine that, the roughly eight months available between the delivery of the President's budget and the beginning of the fiscal year would not provide sufficient time to enact appropriations bills, provided that the Congress viewed it as a significant priority. The fact that the federal government is a large, complicated enterprise, and the federal budget process is a complex process is not a sufficient excuse for this failure.

To begin and end with this conclusion seems particularly unhelpful. For this reason, it is useful to consider some recommendations that start from the assumption that the Congressional appropriations process will not suddenly operate on schedule. If we are stuck with late appropriations, what can be done to minimize their effects?

1. The Congress could make more funding available on a multi-year or no-year basis. At present, many agency salary and expense budgets are provided using one-year money. If agencies had the flexibility to obligate funds over multiple fiscal years, many of the specific problems caused by late appropriations would be reduced. This is not to suggest that all appropriations should permit multi-year or no-year obligations, but it would be useful to specifically review current practice with an eye toward increasing the percentage where such multi-year obligations are necessary. This might assist, in particular, those agencies with lots of grant and contract funding.
2. The Congress might consider prohibiting continuing resolutions, or making them more difficult to enact than regular appropriations. This may seem like an odd recommendation, as it increases the probability of a government shutdown. In fact, it flies in the face of a more common recommendation, which is that failure to enact appropriations should result in an automatic continuing resolution (ACR). The problem is that ACRs may just become the norm; that is, this might reduce the urgency of enacting appropriations even further. Given the problems created by CRs, this would not be a good outcome. Conversely, prohibiting CRs or (for example) requiring a supermajority to pass them would tend to lead to a situation where the options might be either a

full-year appropriation or a government shutdown. Perhaps if there were MORE urgency in enacting appropriations, it would increase the odds of them being enacted.

3. If CRs are to continue, it would be useful if, instead of CRs that freeze spending at the prior year level, the Congress should enact CRs that permit inflationary increases to the prior year level. For those members of Congress and Presidents who believe that spending should be frozen or reduced, this would provide an incentive to reach agreement on appropriations in a timely manner, since the default would be a higher level of spending. For federal agencies, however, this would reduce the necessity of counterproductive actions having to be taken in order to live within a CR that requires spending at the prior year level. This recommendation would also reduce, but not eliminate, the need for anomalies, which should be held to a minimum in the interest of lessening the substantial effort that goes into identifying and negotiating them.
4. The Congress should avoid the temptation to micromanage the budget execution process, particularly if late appropriations are to continue to be the norm. Requirements imposed on some agencies to have spending plans approved by Congressional committees are, in the context of late appropriations, a costly “luxury”. If appropriations were timely, such a review could potentially be justified. In cases where a final appropriation is not received until 3 to 6 months into the fiscal year, there is no justification for the additional delay that such a requirement imposes on federal agencies and their ability to manage funds.
5. Moreover, the Congress and President should limit CRs to only one or two per year that do not extend past the end of the calendar year. It is important to recognize that all CRs are not created equal. It matters how many there are, and it matters how long agencies have to operate under them. Short CRs (especially where there are multiple CRs lasting weeks, as opposed to months) create all sorts of problems for federal agencies that increase the odds of agency officials unwittingly violating some law or engaging in counterproductive management practices. Problems created by attempting to manage through CRs lasting 4 months, or 6 months (or more) are also well documented. If CRs are to be enacted, it is important for them to be enacted in a way that minimizes their negative effects.

It seems particularly important to focus on these improvements at the present time, for two reasons. First, the problem is becoming worse, not better. While historically the problem with late appropriations has been more one of timing than of uncertainty of the eventual funding level, recently federal agencies have

found themselves in a position where both the timing and the amount are in serious question. The recent threat of the Budget Control Act's reductions in discretionary appropriations ratchets up this level of uncertainty to a higher level. Independent of these prospective cuts, the need to reduce federal debt will result in a less than "zero-sum" game for federal agencies; having sufficient time to plan for these budget reductions will be even more important than ever.

My main message, then, is that funding delays have costs. Some of these costs are financial, and others are felt through compromised government effectiveness. Either way, these are completely self-inflicted wounds. The negative impacts are unacceptable given the importance of the federal budget to the overall performance of the U.S. economy and the delivery of services to citizens. The Congress should do what it can to minimize these costs, even if they cannot be eliminated.

Chairman ENZI. Thank you.  
Dr. Ornstein.

**STATEMENT OF NORMAN J. ORNSTEIN, PH.D., RESEARCH  
SCHOLAR, AMERICAN ENTERPRISE INSTITUTE**

Mr. ORNSTEIN. Thanks so much, Mr. Chairman. It is a real privilege to appear in front of this Committee and with a group of people, some of whom I know quite well, who are always working to be a part of the solution and not just a part of the problem.

As my colleagues have said, this is not simply a failure of process and deadlines. There is real damage to the economy and, just as important, to effective governance. We take our Federal managers basically, and it is like putting bags over their heads and handcuffs behind their backs when you cannot even begin to operate knowing whether you are going to be shut down or open or whether you are going to have money for the next month, much less for the next year.

Now, I come to you as a scholar who has also worked inside the Senate on reform issues over many decades with Senators of both parties. In fact, 40 years ago, I was a staff director for a committee that reorganized the Senate's committees, one whose formal name still makes me cringe: The Senate Select Committee to Study the Senate Committee System. [Laughter.]

And I worked with Adlai Stevenson, with Gaylord Nelson, with Barry Goldwater, Bill Brock, Pete Domenici, all absolutely wonderful people. And we had some success. We streamlined the system. We reduced the number of committees and assignments and modernized the information systems. But I have to say, as I look around the Senate, it is not as if this is now a wonderful, efficient body working on all cylinders. And that experience, along with some others in the reform world, left me with at least some level of skepticism about the limits of reform. And we have talked some—and Professor Joyce in his excellent paper and long testimony as well—that, of course, back when we did the Budget Impoundment and Control Act, we changed the fiscal year from July 1 to October 1 because we were not getting appropriations done on time and figured the extra few months would make all the difference. And as you can see from the chart that you put up, Mr. Chairman, it did make a difference. It made it worse. Having the extra time was not effective in a political process where everything would come down to end-game negotiations. So that is a cautionary note, at least.

As Senator Whitehouse said, we could go on about the impact of doing or not doing budget resolutions. I am less concerned about that right now. But to get to a point now where a broad bipartisan budget deal like the one we recently enacted—you recently enacted—is held hostage in the House by a small ideologically driven faction is simply cringe-worthy for anyone who wants to see a functioning legislative process making rational decisions.

So let me talk about a few things that might be done or might not be done, and I want to offer one other cautionary note, which is looking at the process that created the sequester. This is one that was done so that you could have an alternative so horrific that

we would never even possibly consider doing it and force action in the real world by avoiding catastrophe.

Well, we have catastrophe right now, and that suggests to me that we need to be a little bit careful, and that is why, while I agree very much with many of Professor Joyce's recommendations, including especially if we are going to do continuing resolutions they ought to have inflation adjustments built into them, things that would push for action because the alternative would be horrific are not necessarily going to work. A few recommendations.

The first, and one I would emphasize most, is we have got to do something about the debt ceiling debacle that we keep going through over and over again. I was especially disturbed last year when CNN reported that Representative Jason Chaffetz, who was then running to be Speaker of the House, said in an interview that Republicans should be prepared to see a debt default and a Government shutdown in order to pursue their party's agenda. Playing games with a debt ceiling is playing with nuclear weapons, and I strongly recommend that you use the McConnell rule, as it was called, twice used before, and institutionalize it finally, and let the President have responsibility for increasing the debt ceiling and have Congress with the ability to disapprove it with a resolution that could be vetoed. Take this issue off the table, because we are playing with fire with a global economy.

Now, one other recommendation that I would make is that we consider going back—this is the one effective reform that it seemed to me worked extraordinarily well in the 1990s and it was pay-as-you-go budgeting. When we had a process where, if you increased spending, you had to find an offset with revenues or with other spending, it worked, and it worked well. Taking it off the table was one of the worst things that Congress has done, and I strongly urge you to bring it back.

And then, finally, let me say the problem we have here has structural elements, but it is not a structural problem. It is a problem of the norms of governing that we have right now. And now you have a perfect chance with a good, constructive 2-year budget deal. I wish that in that small room the "White House" who had been there was Senator Whitehouse. But the fact is you have got a good deal. And if the House cannot do what it is supposed to do, if the Senate moves and stays within the boundaries of that deal, you are setting an example, and maybe you can begin to change the norms of behavior around here, which is the real problem in our political process.

Thank you.

[The prepared statement of Mr. Ornstein follows:]

TESTIMONY ON "TAP DANCING ON THE RAZOR'S EDGE:  
RESTORING STABILITY TO GOVERNMENT OPERATIONS"

SENATE COMMITTEE ON THE BUDGET

APRIL 20, 2016

NORMAN J. ORNSTEIN

Mr. Chairman and members of the Committee, it is both an honor and a privilege to testify before you today on the need to get our budget and appropriations processes, indeed the broader way we deal with fiscal policy, in order. I am particularly honored to appear alongside two scholars I admire deeply, Philip Joyce and Kevin Hassett.

I come to you as a scholar who has also worked inside the Senate on reform issues, and worked over many decades with senators of both parties on these issues. Indeed, forty years ago, I was the staff director for a committee that reorganized the Senate's committees, one whose formal name still makes me cringe: The Senate Select Committee to Study the Senate Committee System. Among those I worked with closely were Adlai Stevenson, Gaylord Nelson, Barry Goldwater, Bill Brock and Pete Domenici.

In that effort, we succeeded in eliminating some committees and subcommittees, streamlining jurisdictions, reducing assignments and modernizing information systems. But, as is pretty evident looking around the Senate today, those changes, worthwhile though they were, did not transform the Senate into a focused and efficient body. That experience, along with other reform efforts in the years since, have left me with a healthy skepticism about the limits of structural reform in a body that is inherently political, and with a deeper realization that in many if not most cases, the norms of the body and its members—their willingness to follow the regular order, even while gritting their teeth, to put, at least occasionally, the long term needs of the polity ahead of short term political gains or points scored—trumps structural change.

Of course, there is no doubt that our processes are now profoundly dysfunctional. When it comes to manipulation of the debt ceiling, we are not just playing with fire—we are playing with nuclear weapons. The typical and costly uncertainty attached to spending bills has been replaced with deeply destructive swings that often make it impossible for federal executives to plan for the next day or week, much less for a single year or to develop reasonable five or ten year plans. The periodic threats of shutdown mean that almost every year, managers have to stop managing or planning the implementation of their programs to plan instead for a stoppage. No organization, public or private, would opt to function without some reasonable level of certainty and predictability in budgeting, much less with the regular threats of turning out the lights. But for years, now, agencies have had to cope not just with these uncertainties but with mindless across-the-board budget cuts that hurt most the efficient, lean and mean



programs and that hamper national security, homeland security and economic security, among other essential things. And frankly, if we add to those challenges the attacks on the integrity of federal workers, including the pay freezes and bans on attending conferences or doing continuing education, the threat to effective governance is multiplied.

I am less concerned with the erratic pattern of passing budget resolutions, which are often far more symbolic than real, and which have turned into hyper-partisan exercises that become even more embarrassing when the majority party can't even find a majority among their own members. I am aware that budget resolution deadline day was five days ago, with no resolutions in sight. But to get to a point now where a broad, bipartisan budget deal like the one recently enacted is held hostage in the House by a small ideologically driven faction is simply cringeworthy for one who wants to see a functioning legislative process making rational decisions about policy and priorities.

It is understandable that the Budget Committee wants to find ways to change things, to move from dysfunction to functionality, to enable a process where whatever one's views about the appropriate size of government and size of the federal budget, the government that we have functions well and serves the collective interests of the American people. But the members of the committee need to be aware about the limits of reform and the underlying nature of the problem even as you work towards change.

The limits of structural change on fiscal policy are made evident by a point Professor Joyce makes in his paper, "The Costs of Budget Uncertainty," a point I make regularly when talking about reform. Before the 1974 Budget and Impoundment Control Act, the fiscal year began July 1, leaving less than six months to enact spending bills for the coming year. The Budget Act added three months, moving the date to October 1, with reformers assuming that the extra time would make it much easier for Congress to complete the 13 appropriations bills on time. The opposite happened. Why? Because spending bills are at base core priority decisions, which are driven as much or more by politics and ideology as they are by objective or technical criteria. That means that strategic endgames often take precedence over artificial timetables. I should note here that this reality should make us a bit cautious about the impact of a very popular reform, moving to two-year appropriations. I would be perfectly happy to have many spending decisions taken off the roller coaster with longer-term appropriations, but also believe that it could and probably would lead to manipulation of assumptions and probably higher stakes end-game negotiations and brinksmanship.

In some ways, the starker reality of the limits of structural remedies emerges with the advent of the sequester. The process that framed the most significant budget negotiations in many years was designed specifically to force broad bipartisan agreement on long-term fiscal policy—by creating an automatic alternative if negotiations failed so stupid and destructive that it would simply be unacceptable to all parties. Those mindless, across-the-board cuts in defense that would over time absolutely cripple national security would push Republicans to compromise;

the mindless, across-the-board cuts in agencies like NIH and CDC would push Democrats to an agreement as well.

It was a powerful theory. But the failure to find that common ground—driven especially by the unwillingness to consider significant revenue increases as part of a package of budget cutbacks in both discretionary and entitlement programs-- showed that the theory was hijacked by the ideological and partisan reality of our time. Thus, I have to conclude that any reforms designed to make the outcome disastrous if Congress does not belly up to the bar and do the right thing—including eliminating continuing resolutions—would in the current dynamic lead to more disastrous outcomes.

So, what to do? There are, in fact, some reforms that would be highly beneficial to enact. The most important is on the debt ceiling. We all know that both parties have played politics with the debt ceiling for decades, with roles switching depending on the party of the president. But it is also clear that for most of the period since the debt ceiling was created in 1917, the games were basically fixed. All the party leaders, and most of the rank-and-file members of Congress knew that when push came to shove the votes would be there to insure that the full faith and credit of the United States was preserved and the debt ceiling would be lifted; I had many party leaders tell me that they had the votes in reserve from those who had scored political points back home by declaring their fiscal discipline and vowing not to increase the debt via an increase in the ceiling in case they actually needed them.

But in the Obama years, the game changed. I found it particularly disturbing when, in 2011, Senator McConnell said, “I think some of our members may have thought the default issue was a hostage you might take a chance at shooting,” he said. “Most of us didn’t think that. What we did learn is this — it’s a hostage that’s worth ransoming.” I was even more disturbed when CNN reported that Representative Jason Chaffetz, running to be Speaker of the House, noted in an interview that “Republicans should be prepared to see a debt default and a government shutdown in order to pursue their party’s agenda.”

I understand political games. But this is potentially catastrophic for the country and indeed for the global economy. So I would urge you to institutionalize the so-called McConnell Rule, one the Majority Leader to his credit instituted in both 2011 and 2013 when he decided it was more beneficial to punt on the issue, to enable the president to increase the debt ceiling, with Congress having the power to pass a resolution blocking the action and the president able to veto the resolution. Our national debt is shaped by the actions taken by Congress on spending and taxing; those actions raise the debt, and an artificial ceiling, a practice shunned in almost all other mature economies, is deeply unwise and subject to very bad consequences.

On other reforms, including those proposed by Professor Joyce, I particularly commend the idea of ensuring that CRs include inflation adjustments; the failure to do so not only punishes programs the way sequesters do, but provide incentives for members who are less concerned

with the regular order and more concerned with slashing spending, no matter how mindlessly, to block appropriations and go for CRs.

I want to conclude with a broader plea. The big problem we have in our politics right now is not polarization. As the longstanding example of the odd couple partnership between Ted Kennedy and Orrin Hatch proved, you can make good public policy with partnerships from the poles. It is the breakdown in norms and in what we mavens of the legislative process call the regular order. The changes in the use of the filibuster over the past decade occurred while a version of Rule XXII that had been in effect since 1975, and worked well for more than 30 years, began to be distorted for purposes for which the rule had not been intended. The breakdown in the budget process, including budget resolutions, enhanced brinksmanship, government shutdowns, failures to meet deadlines, the decline of broadly bipartisan appropriations bills, and the use of the debt ceiling as a hostage, was more because longstanding norms of behavior deteriorated than because the process was faulty.

Indeed, you now have a near perfect chance to show how a change in norms to focus on the regular order will dramatically improve things. We have a two-year budget deal set with broad bipartisan approval, one that creates workable caps around which to build a dozen appropriations bills, with the time to complete them before October 1. There are no structural impediments in either the House or Senate. Of course, we know the House is a bigger challenge, but the votes are there for majorities for the spending bills—although they cannot likely be done with one party alone. The Senate, however, should be able to pass these bills by broad majorities with ample time for conferences, to show the House an example of how Congress can make the process work when the will is there.

So feel free to consider and make salutary structural changes. But please, at the same time, look inward and change behavior.

Chairman ENZI. Thank you. I thank all three of you for your comments and for your written testimony, and your entire written testimony will be a part of the record, and I appreciate the items that are in there as well.

Senator Whitehouse and I have agreed to defer on our questions so that those of you who showed up can have an opportunity here, so we will begin with Senator Corker.

Senator CORKER. Thank you, Mr. Chairman. I do that a lot on the Foreign Relations Committee. And I appreciate, first of all, your leadership on focusing on budget reforms, and I appreciate the opening comments of Senator Whitehouse, who generally agrees that we need to figure out a way to reform the process. And I want to thank David Perdue, a new Member of the Senate, for his efforts on both sides of the aisle to try to create a process that works, and then say that I lobbied to be on this Committee. And after being on it, I have to say our budget process is the biggest hoax cast upon the American people and Congress that I have ever been a part of. And to vote for a budget challenges one's integrity and certainly one's intellect.

The fact is we say grace over about 30 percent, 33 percent of the spending each year. We put in place assumptions that are never going to be reality and have no policies whatsoever to back them up.

So I thank the Chairman for his leadership in changing that because, again, it is a shame that the American people even believe there is a budget process that has something to do with fiscal discipline. As a matter of fact, because it is a political document—and when Republicans are in charge, we stress Republican priorities, and when Democrats are in charge, they stress Democratic priorities—we actually spend more. It actually causes us to spend more. So I want to thank all involved for the process.

Let me just ask the panel, you know, right now the budget is a resolution. It is not a law. Not a law. So we are never forced to make the difficult decisions that need to be made where both sides have to come together. Whoever is in charge just passes a budget with no real input from the other side.

Would the three of you agree that we would be much better off if the budget was an actual law that forced the two sides to have to get together and make difficult decisions about the future of our country?

Mr. JOYCE. Let me start by saying that I agree that if the budget had more teeth, it would be a better thing. My concern about making the budget resolution a law is that we already have enough trouble getting the House and the Senate to agree on a budget resolution. If we involved the President, it might just increase the chances that you would end up without a budget resolution.

Senator CORKER. Would it not make sense for everybody on the front end to agree to the tough decisions? There is no forcing mechanism right now. None. The fact is we spend money we do not have. Angus King and I had dinner once, and he was asking me if a tax decrease when you have a deficit is really a tax decrease. It is really not. It is a tax increase on future generations.

So, in essence, there is no forcing mechanism to force the two sides into making tough decisions, and so as long as it is a resolution, it has no real impact. We have budget waivers.

What is the forcing mechanism? What is the forcing mechanism around here to force Congress to deal with the fact that when this meeting ends, our Nation is going to be less well off than it was, it is going to be a weaker Nation because we do not have the forcing mechanism—or maybe it is courage—to actually address the issues that we need to address? Name a forcing mechanism.

Mr. ORNSTEIN. Well, reconciliation in some ways is the forcing mechanism. It is a very, very, very bad one, an imperfect one. But I think, you know, the problem, if you make it a forcing mechanism, is that it is then going to be a law that will have to go to the President. And that can be vetoed, and you are going to have some difficulties.

And what I would suggest, Senator Corker, is really go back and think about the pay-as-you-go mechanism that we had in the 1990s. Study it and look at it, because that was a forcing mechanism. And it was—if you want to increase spending in one area, you are going to have to find an offset.

Now, it was taken out because the offset included the ability to increase revenues to make that offset and not just cut spending in another area. But the fact is it brought forcing a discipline to the process.

Senator CORKER. Well, let us talk about that——

Mr. ORNSTEIN. There is a way to do it, and not necessarily with a budget resolution.

Senator CORKER. Well, first of all, thank you and I appreciate your many contributions in so many areas and the way you have worked with our office. Let us talk about PAYGO. So you spend money for 1 year on something, and you pay for it over 10. Now, is that rational? That is the way PAYGO works. It is a hoax.

We should be ashamed—ashamed—that the way we deal with Americans' money—but let us go back. Again, PAYGO, is that a sane process where we are going to spend \$10 billion this year, but we will pay for it over 10—by the way, with a bunch of gimmicks. But is paying for money you spend in 1 year over 10 a sane way of doing business?

Mr. ORNSTEIN. I am very happy to cut a deal where you pay for it the same year that you——

Senator CORKER. I could not agree more. I could not agree more.

Mr. ORNSTEIN. And that would be just fine. So it was imperfect the way it was done, but it did bring discipline.

Senator CORKER. My time is up. I appreciate the testimony.

Chairman ENZI. Thank you.

Senator Murray.

Senator MURRAY. Thank you very much, Chairman Enzi. Thank you to Senator Whitehouse for standing in as Ranking Member today.

I also want to thank all of our witnesses who are here today, but before I ask my questions, I think it is important to put this hearing in some context. It was not too long ago that Congress was pushing our country from one crisis to another, one artificial cliff to the next, debt limit scares, threats of across-the-board cuts. And

then as we all know, in 2013 a minority of Republicans pushed us into that 16-day Government shutdown that hurt the economy, disrupted the Government's ability to serve families across our country, and made a lot of our constituents doubt that Congress could work together to do the job that we were elected to do.

So I am very proud that after that Government shutdown ended, then-House Budget Committee Chairman Paul Ryan and I were able to sit down in a conference and work to get our budget process back on track. We knew we were not going to be able to solve every one of our budget challenges then, and we knew there were some deep partisan divides over core budget issues that we were not going to bridge right away. But we both agreed we owed it to our constituents and to our country to find a way to work together, make some compromises, and reach an agreement. And with the help of many of our colleagues here on this Committee, now-Speaker Ryan and I reached that 2-year budget deal that prevented another Government shutdown. It restored investments in education and health care and research and defense jobs and other middle-class priorities and really showed the people across the country that their Congress can work together and get something done.

Now, after that 2-year budget deal ended, we built on it at the end of 2015 with another bipartisan agreement that once again restored the across-the-board cuts and allowed the Appropriations Committee to now do their work. So we are in a better place than we were just a few years ago, but there are significant challenges ahead of us.

Some members of the Republican Party, especially in the House, now want to ignore that bipartisan deal of a few months ago and force additional massive cuts that we know will hurt our workers and our families and the economy, and there is no so much disagreement between Republicans in the House and Senate, they may not even pass a budget this year—I would say despite sending many messages when Democrats were in charge about how important it was to pass a budget every year. I just have to say this: “No budget, no pay” came from Republicans. Now that you are in charge, we do not hear that. But I understand. It is always easier to be in the minority than the majority around that.

But, still, given the dysfunction that we are seeing this year, it is not surprising we are here to talk about the budget process as if the process is somehow responsible for the Tea Party and the Freedom Caucus.

But a lesson I took from my deal with Speaker Ryan is that we need more than process changes to get this budget back on track. We need Members of Congress to understand that the only way we can work for our constituents is by working across party lines and actually trying to get something done. Partisan budgets that make those dramatic cuts on paper to appease one side or the other have no basis in reality of making sure Government actually works for the families we serve, and it is the wrong approach. We need to take the lessons from what has worked and work together to put families and the economy before politics and partisanship.

But as we are here today to discuss these process issues, I am going to be very focused on making sure we do not make changes that actually hurt the ability to invest in non-defense priorities or

call on the wealthiest Americans or largest corporations to pay their fair share. And I believe that even though our 2-year budget deals show how multi-year budgets could work to encourage bipartisan agreements and avoid artificial crises and increase certainty in policymaking, we should not set aside the important oversight role that Congress does play through the annual appropriations process and the ability for Congress to use the power of the purse each year to examine and to challenge and to reassess the needs of our agencies and our programs.

So I just have a few seconds left. I am sorry. But I want to just start with Dr. Ornstein. What can Congress, and specifically this Committee, do to build on the foundation laid down by the Murray-Ryan budget deal 2 years ago?

Mr. ORNSTEIN. I really commend you for that deal, which really was an extraordinarily constructive act that you and Speaker Ryan did.

Let me say first the no-budget, no-pay idea is one of the stupidest things I have ever heard, even though it actually came from Senator Corker's colleague and my friend, Jim Cooper, first. But the idea that you do collective punishment and give enormous leverage to the wealthiest Members of Congress who do not care if they do not get paid just does not make a lot of sense.

But it seems to me that what we need in that case is not a structural change so much as it is right now a massive commitment, from not just the Senators in this room but everybody else, that you are going to take the model there and the model from this new deal and you are going to put through appropriations bills on time that fit the budget framework and send them as quickly as possible over to the House. And then we can put public and other pressure on the House to do what it is supposed to do.

This is a breach of norms as much as anything else. These other structural changes, we should be thinking about making them, but right now, in the short run, it is that.

Senator MURRAY. Okay. And I am out of time, and I apologize, Mr. Chairman. But I look forward to hearing your responses in writing, so thank you.

Chairman ENZI. I thank you for your comments and took from that a suggestion that we do biennial budgeting.

Senator MURRAY. As I said, I want to be very careful that we look at the appropriations process and recognize that the oversight work we do each year in Committee and evaluate whether, you know, we have got an appropriations bill with a program that, you know, should not be funded anymore, we do not lose sight of that in a 2-year budget deal, that we have the ability every year to analyze this, Members of Congress, whether something is working, and eliminate it or add to it, if we all agree to.

Chairman ENZI. One of the suggestions we had last week was that we become a National Priorities Committee instead of a Budget Committee and concentrate more on that oversight area where people are not doing it.

Senator Perdue.

Senator PERDUE. Well, Mr. Chairman, you know, in these hearings, I am amazed. I continue to be just absolutely dumbfounded.

First of all, I want to congratulate you and Senator Whitehouse. There is something going on here that I want to comment on very positively, and that is, I sense a sense of bipartisanship in this Committee. I look at the members who are here. Most of them who are here are generally at these hearings about changing the budget process. I want to applaud Senator Murray for her prior work and focus on this. And, Senator Whitehouse, God help me, it sounds like he and I are agreeing on a lot of things in the last few meetings about how to move forward. [Laughter.]

Senator WHITEHOUSE. You better go check with your staff.

Senator PERDUE. Yeah, really. [Laughter.]

But having said that, I want to make a couple comments.

First of all, there is \$6 trillion not in this economy right now because of our malfeasance—\$2 trillion sitting overseas in unrepatriated tax; \$2 trillion on bank balance sheets—we could argue why it is there, but it is there, the largest history; and \$2 trillion on Russell 1000 balance sheets because of the uncertainty you gentlemen talk about.

I am just a dumb business guy, but I can tell you, it is real. I would not invest in this environment. And they are not. And that is a huge drag on this economy. We have got two Governors sitting right across from us, and they both have run great governments and in fiscally responsible ways.

What we are doing right now, we have no planning, no capital budget, no balance sheet. We have cash accounting and accrual accounting in different parts of our Government. We have a DOD which is the single largest budget, I think, outside of the mandatory expenditures. We cannot even audit it.

Call Wal-Mart and explain to them it is okay to call the SEC next year and, say, "By the way, we are too large to be audited. We will see you next year." It cannot happen, right?

This is unbelievable. We have a budget process that has only worked four times in 40 years. That is not a partisan statement. Four times in 40 years. I apologize, Dr. Ornstein. I know you were part of that. But honest to God. I have read every word of this a couple of times. I cannot see how this could ever work. And it only worked four times in 40 years.

It is time that we do, I believe, a clean-page approach to this. This is not about tweaking around the edges. This has a fundamental flaw, and that fundamental flaw is this: We have a budget resolution that requires 51 votes.

Now, I have got to tell you, both sides are guilty of doing this, and it is going to continue. It is not going to stop by somebody's good behavior. I think we have to change that from a budget resolution to a budget—so what happens with 51? The majority crams down the throat of the minority every year a budget. Then we go to authorization. When was the last time, Mr. Chairman, we authorized anything in this Senate? I cannot remember. In 13 years, we have not been able to get a State Department reauthorization. I know that fact.

So then we push it to an appropriation. Why would a minority ever let the majority cram down an appropriation in its entirety when it can wait and get a CR and go into an omnibus conversation that Senator Whitehouse just perfectly described? Why would



a minority ever do that? We did not do it when we were in the minority. The Democrats do not do it when they are in the minority.

Look, Madison did a great job of protecting the minority. He did a great job. Here is one problem where we have got to change that, in my opinion. And I could not disagree more with the idea that there are not severe consequences to the people in this room and the people in the United States Senate if we do not fund the Government. This is not a budget process. It is a funding process.

We get confused here this year thinking we have—I have heard leaders of the Senate talk about we are in a budget process because of the appropriation process that we are about to start. That is not it. Budget authorization appropriation really does not work. It is the only institution I can find in the world that basically does those three steps in a discrete manner. We have looked. And what I think has to happen is that we have got to have severe consequences for not funding the Government in an appropriate amount of time. I think the fiscal year does need to be changed. I can make a large argument right now that every new Congress starts 3 months behind. And we have got an appropriation process that takes too long, too much calendar time with the rules of the Senate to do 12 individual bills.

This, gentlemen, I want to submit it to the record. This is what we have right now from a Committee structure. It has been changed over the years, but we have about 16 authorizing committees that do not authorize, and we have 12 Appropriations Committees over here—and, by the way, there are very few—I cannot see but one—well, there is not one. There is not a one-to-one relationship between any funding committee and any authorizing committee. Not one. Now, that is wrong.

We have got to start somewhere, and I really believe that what we have an opportunity to do right now this year, because of what the Chairman has said—Senator Murray alluded to it. Senator Whitehouse said it a week ago in another hearing, and he repeated it today. I think we need to have a nonpartisan conversation about a party-neutral process to fund the United States Government.

I see heads shaking. I know you have tried to do that. But the thing that breaks down here is that we want to put issues on it like spending caps. I agree, we need to have that debate. We need to have things about discretionary spending. I agree 100 percent. There are programs we have got to protect. We have got to get mandatory into the conversation. How can we call ourselves funding the Government if we do not talk about every dollar that the Federal Government spends?

So these are fundamental guiding principles that I believe we can find commonality if we keep the party partisanship out of here. And my question to you guys is basically—Dr. Ornstein, I respect your work so much. I have read much of it. All of you have great pieces of work, great thoughts in here, and have made huge contributions. We need your help. You do not have time to answer this question, but I would love to have you respond to this question in writing. Give us a one-pager of your priorities of a clean-page approach that could help us—you know we are going to have partisanship here. There is no way to get around that. We are going to have a majority; we are going to have a minority. We are going

to have all the human frailties. But sooner or later, we have got to have a process where we can fund the Government.

I apologize. I really had some really good questions, but this is the one I would love for you to respond to: How would you approach a clean-page approach? I would love to have that for the record. Thank you.

Senator PERDUE. Sorry, Mr. Chairman. Thank you.

Chairman ENZI. And we will allow you to submit your other questions as well or stay around for a second round.

Senator PERDUE. Thank you, sir. I appreciate it.

Chairman ENZI. Sure. Thank you.

Senator King.

Senator KING. Well, I first want to begin by associating myself with Senator Perdue's comments. I think he has outlined the problem magnificently and dismally. It is not a happy picture.

I also want to take off on what Senator Corker mentioned. When you include tax expenditures, we are really only fighting here about one-fourth of the budget. We are spending all of our time on really one-fourth of the Federal budget when you include mandatory expenditures and tax expenditures, which most economists consider the same as expenditures. And that really makes the process even more sort of puzzling that we are—my mother used to say we are straining at gnats and swallowing camels. And that is essentially what we are doing. So that is number one.

Number two, it seems to me that whatever process we devise has to be forward-looking in terms of long-term impacts and long-term trends. If you project out current expenditures in the mandatory area, it basically squeezes out all of the discretionary budget over the next 20 to 30 years, particularly if you maintain a tax cap, what amounts to a tax cap.

PAYGO I think did work, largely, in the 1990s. I do think if it is going to be applied, it has got to be applied both ways. It has got to apply to both expenditures and tax cuts. Otherwise, you end up in the same kind of hole that we are in now.

On the debt ceiling, I have always thought that there should be a kind of automatic debt ceiling extender in spending bills because right now we are allowed to have it both ways. We can vote for spending bills and brag about the consequences back home and all the good spending that we brought home to the local airport or sewer plant, and then vote against the debt ceiling and call ourselves fiscal conservatives. If you vote for the expenditures, you ought to be at the same time voting for an extension of the debt ceiling, because that is what you are doing when you make those expenditures. As we all know, the debt ceiling is an easy issue to confuse people about. The debt ceiling is to authorize the borrowing to pay bills that we have already incurred, that we have already spent. So when we do the spending, it seems to me that is when we ought to do that, and it would take that nuclear weapon off the table and I think improve things significantly.

Norm Ornstein, you have nodded several times. Do you agree on PAYGO, that it has to work both ways?

Mr. ORNSTEIN. Absolutely. It does not work unless it works in every direction. And I agree with Senator Corker that you cannot basically manipulate it so that you are spending in 1 year and then

you are taking 10 years and stretching it out and using all kinds of gimmicks. But it has got to work with taxes as well as it does with spending.

Senator KING. I was amazed when I got here that somehow, when you get inside the Beltway, the law of net present value does not apply. There is no concept of net present value. A dollar saved 10 years from now is equal to a dollar spent today, which, of course, any businessperson or economist will tell you is absolute nonsense. But that is something that we really ought to be talking about, is applying net present value concepts to this whole PAYGO idea. I think PAYGO ought to be a year-to-year deal.

Mr. ORNSTEIN. And in an ideal world, you would not even have to have a debt ceiling debate or issue. It is absolutely something that you build into spending or into—as we actually did for a few years with what was called the “Hoyer rule” in the House, where it was automatically extended when you did a budget deal, because you are making those decisions.

There are some things that could be done here that would make a difference, and I cannot think of anything that would make more of a difference than if you devised a PAYGO package that was honest and real and disciplined. And I do not think it is impossible to do that.

Senator KING. And if you did that, you would not be necessarily in a balanced budget because it would depend on the baseline you started with, but you at least would not be making things worse. Then we need to talk about—and I hear no talk about this: How do we deal with the \$18 trillion debt? I mean, balancing the budget would be nice, but we have still got an \$18 trillion debt. And somehow we need to start talking about how that is reduced, and I do not know whether—I do not know what the mechanism is, but—perhaps economic growth is the answer. But we have got to be dealing with that problem in addition—I mean, getting the deficit to something close to a balance is ceasing to dig the hole. But it does not deal with the depth of the hole that we have already dug over the last 25 years.

Thank you, Mr. Chairman. I yield the floor.

Chairman ENZI. Thank you.

Senator Kaine.

Senator KAINE. Thank you, Mr. Chair, and thanks for holding this hearing. And to the witnesses, I appreciate your scholarship and your insights. And I have got to give a special praise to Dr. Joyce. When you have a University of Maryland professor who is spending as much time helping Arlington County, Virginia, as you do, with the school board and other—I have got to note that, and thank you for helping my Commonwealth.

A story. So last Monday I decided to go and shine a spotlight on the National Park Centennial, and I went up to Shenandoah National Park to go on a hike with employees there. And I sat and had coffee with them for a while, went on a hike, and then had lunch with a bunch of community leaders. When the superintendent of the park stood up, he said, “Not only is Tim Kaine a great friend of the parks”—and I do a lot of things in the parks. He said, “But, Senator Kaine, thank you for that 2-year budget.

Thank you for two 2-year budgets in a row. You have given us some certainty that we need.”

We have done two 2-year budgets in a row. Now, they have got a lot of warts on them. It was kind of painful getting there. The first one only came after a shutdown of the Government, and the second one, arguably, required the retirement of a Speaker to get done. I am not sure we can count on that every year, on those kinds of cataclysms. But we have done two 2-year budgets in a row that have provided some certainty, and I am hearing it when I talk to the DOD on my Armed Services billet. When I talk to the Park Service, our internal folks are saying, “You have given us some certainty.” And when I talk to my outside community, the private sector community, they say, “Stick with the 2-year budget deal because you have given us some certainty.” And it looks like that we are kind of on track to stick with the 2-year budget deal. The allocations have been handed out to the various Subcommittees on Appropriations, and it looks like we are going to try to stick with the deal, which is great.

You know, any Governor, mayor, we are kind of certainty fanatics. We want to give people some certainty, and they are not going to like everything they see. They are going to argue with us about all the line items. But they would rather have a line item that they did not like than have a big asterisk or a question mark.

So I think part of what we need to do on the reform side is we are taking baby steps towards certainty, and we still have a lot of problems, but let us keep doing that. And I will say to Senator Murray’s point—she is gone—that that thank you from the NPS to me, they recognized we have done a 2-year budget and it is still single-year appropriations. But they are okay with that because they kind of get, once the first-year appropriation is done, as long as we stick with the budget deal, the second-year appropriation will be kind of range of reason, and that gives them enough to be able to predict about. So we can make this work.

Here is a certainty thing I am interested in, and I am curious as to your thoughts about this. What is the forcing mechanism? I will tell you what the forcing mechanism is when you are a mayor or a Governor. I have been both, and I have had the same forcing mechanism both times, and it was simple. It was an agreement upon a debt management policy.

The whole notion of debt as just a dollar amount is ridiculous. It is ridiculous. And that we have a debt ceiling thing set at a dollar amount, it is economically so unsophisticated. You have a debt management policy that is usually around total debt as a percentage of local, State, or national GDP and debt service payment as a percentage of the annual outlay. That is how we managed it as mayor; that is how we managed it as Governor.

And the interesting thing was this was a bipartisan consensus. It was not a law. It was not a requirement. If we violated it, we were going to get downgraded in our bond, so that was sort of the umpire we were trying to kind of look at. But we agreed on the policy, and that left so much room for normal partisan debate. There is a policy. That is fine. How do you get to the policy? Then the Dems would argue we have got to have more revenue. The R’s

would argue, no, you have got to cut more. We would come up with an answer, but nobody questioned the basic policy.

So I was quite surprised to get here as a Senator and find that there is really no debt management policy. We had a hearing about a year ago that the Chairman called, and the title of it was "America's Dangerous Debt." And when I asked all three of the witnesses, majority and minority, "Okay, America's dangerous debt, what level of debt is dangerous? You tell me." None of them would even give an opinion about what the metric should be to determine the line between acceptable and dangerous debt. We do not have a debt management policy.

If you have a policy, you can provide plenty of room to argue, partisan or otherwise, about how to get there. But if you do not have a policy, it really means there is not a forcing mechanism. We would be much better off having a debt management policy expressed as ratios and scrapping the whole debt ceiling thing in terms of dollars. Because when we say to the American public we have \$18 trillion in debt, they are going to freak out because that is a big number. But you can imagine the size of an economy where that level of debt would not be dangerous. Or you can imagine an economy where \$1 trillion of debt would be super dangerous. The raw number is meaningless, but that is part of the hoax that we are perpetrating, we are managing by a meaningless number and refusing to develop meaningful measures.

So I would be curious. States and Feds are different because States only use debt for capital, and Feds use, and should, national governments use debt for capital plus operations. But I think maybe I am just going to ask this for the record because I would like your considered thought: Could we have a Federal debt management policy? And in your expert opinion, what would it look like? And I am out of time, but I am going to ask that question for the record, and I would love to see your answers.

Senator KAINE. Thank you, Mr. Chair.

Chairman ENZI. Thank you. What a great bunch of suggestions and ideas. I have got a lot to kind of digest through the rest of the day and the week as we work toward next week. But I have got a few questions, too.

Dr. Joyce, you mentioned in your testimony that late appropriations produce significant costs, and many of the Members of Congress, both Democrats and Republicans, have suggested moving to a 2-year budget cycle to provide certainty and stability in the appropriations process.

Now, what we have actually talked about is a 2-year budgeting process, not a 2-year appropriations process. I want to make that distinction. What do you think that a 2 year appropriations cycle would do to affect the uncertainty? Do you think that would be a possibility based on your previous experience and study?

Mr. JOYCE. Well, I would say that, you know, as you noted, I was at CBO for 5 years, and during the 5 years I was CBO, I probably wrote ten testimonies on biennial budgeting. So this is an idea that has been around for a while. And I have testified a couple times on biennial budgeting since then.

I would say that on the topic of this hearing, which is certainty, there is no question that, as Senator Kaine suggested, knowing

what your number is for more than 1 year is something that is beneficial in terms of the management of Federal agencies. I think that the question that one has to ask is whether what is a biennial appropriations process on paper will end up being an annual process in fact. That is, will there be such big changes in what is theoretically the non-budget year, you know, that it sort of offsets the effect of that improvement in certainty.

In terms of the biennial budget resolution, you know, you have to admit that it would be an improvement over what we have now because we do not even do a budget resolution every other year. So if you really sort of stuck to it, it would be a good thing.

I do think that while we are in budget disequilibrium, as we are now, you have to admit that it would cost you the opportunity every other year to use the reconciliation process if you thought that is what was necessary in order to try to come up with whatever the big deal was that would bring the budget back into equilibrium.

Chairman ENZI. Thank you. Of course, one of the suggestions was that reconciliation only be used for debt reduction, and the appropriators have all said, "It would be good to have a biennial budget, but do not make us do biennial appropriations." And that is because everybody likes to give away money every year, and that is a part of the problem.

Another part of the problem, of course, is if we go to biennial budgeting, probably the best time to do it would be right after an election. Right before an election, people are all concerned about whether they will get reelected if they are really tough on spending or taxes or anything. The difficulty with doing it right after an election is that every 4 years it will have just—a President will have just been elected who will not have had the Office of Management and Budget working for him and so will wind up with a document—it is about 2,500 pages, which I am not sure anybody ever looks at—that that President would not have put together. I am not even sure whether any President has looked at all of those pages that have been put together for him by the Office of Management and Budget.

Senator WHITEHOUSE. Ever.

Chairman ENZI. Ever, right. So getting the President into the process, one of the things that was suggested was having the President, instead of presenting all the numbers, present what he wants to achieve over his 4 years, and instead of budgeting for 10 years, budget for 4 years, and see how many of those priorities can be worked in there, both additions and subtractions, to get a PAYGO over a 4 year period, which would be more beneficial than a 2-year period.

Would either of the other two of you care to comment on any of those comments?

Mr. ORNSTEIN. I wrote a couple of things a few years ago on 2-year appropriations and a 2-year budget, partly at the urging of Pete Domenici, who was so ardent in this area, and he was such a good person that I decided I would do it, but with misgivings, especially about 2-year appropriations.

I do not think 2-year appropriations ultimately will work because they just do not fit into the political needs of members. And you

end up with the end games that we always end up with, which is why changing the fiscal year, nice as it might be, is not going to effectively do very much. And the longer you extend those, the more games are going to be played with them, and the more adjustments will be made along the way.

But having said that, I think what Senator Kaine said is powerful. And I would add, Mr. Chairman, if you do not mind, I really think we have to focus on how we can make the Government that we have work effectively and efficiently, and there are too many members who want to blow the whole damn thing up. And this goes beyond giving managers some certainty so that they can plan ahead. It also gets to how we are now cutting out every ability for people to do continuing education and training. We are cutting their pay or freezing it for years at a time. I think we have to have an even broader focus.

Whatever size of Government you want—and we are going to have differences, all of us, as all of you will—what we have should work well. And there, 2-year planning clearly is a better idea if we can make it work somehow.

Mr. HASSETT. Mr. Chairman, I would like to go back to what Senator Kaine said. My view is—and Norm knows this is something that I have been pushing for a while—that the right thing to do is to have an argument or a debate about what is the appropriate—what would a reasonable budget look like? What is the appropriate level of Government spending to GDP? What is the appropriate level of taxes to GDP? What is an appropriate trajectory for the deficit? And then you would—of course, we would not agree about the point estimates for that, but we might agree about a range. Like we do not want to have debt to GDP exploding. Maybe if it is above X percent of GDP, if it is above 20 percent of GDP, the spending, then that is something that I would not like. Or we could argue about it. But once we set those parameters, if the budget that you pass meets them, then it ought to be that continuing resolutions and debt limits happen automatically.

I think that that is the way I would construct it, not lean on PAYGO, because then you guys could decide what you think is a reasonable budget, and then if a budget is passed that is reasonable, then all the things that we are worried about—again, we are talking about 2 years as opposed to 1 year, in part because we want to avoid the cliffs and the shutdowns and the games of chicken. But if the budget process basically has a debate, an honest debate, lots of hearings about what does a reasonable budget look like, and then you guys decide this is a reasonable budget, and if we meet those parameters, then we are not going to have those shutdowns, then I think that we will have improved the process.

Chairman ENZI. Thank you. My time has greatly expired.

Senator Whitehouse.

Senator WHITEHOUSE. Thank you, Chairman.

Let me make just a couple of points, and I think what we are trying to do is build a record here for us to get together. So if you will respond not only to the other questions but to these points, the first one with respect to the concern about continuing resolutions, if the appropriators are free to appropriate when authorizations either do not exist or are expired, then the CR becomes a very easy

thing to manage around. And so what the heck? So appropriations discipline should have some pushback into making continuing resolutions less awkward. On the other hand, if you are going to have to live by continuing resolution, it is practical to have the appropriators make those adjustments as you continue to bring kind of zombie programs over and over again through time.

I assume you gentlemen know what the size is of the national debt.

[Witnesses nodding heads.]

Mr. JOYCE. Yes.

Senator WHITEHOUSE. Give the number.

Mr. HASSETT. I have got it right here in the chart I just—

Senator WHITEHOUSE. Give the number for the record.

Mr. HASSETT. The debt held by the public as a share of GDP at this exact moment is about 78 percent—I am looking at a chart, a graph.

Senator WHITEHOUSE. In dollars?

Mr. HASSETT. Excuse me?

Senator WHITEHOUSE. In dollars? In trillions of dollars?

Mr. HASSETT. Oh, now we are testing me a little. Yeah, so—

Senator WHITEHOUSE. I have it as 19—

Mr. ORNSTEIN. \$18 trillion, I think? It is somewhere around \$18 trillion.

Senator WHITEHOUSE. Yeah, \$18, \$19 trillion. Okay.

Mr. JOYCE. That is the gross debt, yes.

Senator WHITEHOUSE. That is the gross debt, exactly.

Now, we budget here on a 10-year budget cycle. How much money goes out the back door of the Tax Code through tax spending over a 10-year budget cycle? If you do not know, it is about \$20 trillion, which means that if we could manage our tax spending better, we could have a very big mechanism for getting rid of the debt. The total national debt is less than goes out the back door of the Tax Code every single 10-year budget cycle.

So part of what we need to do, I think, in budget is make sure we are addressing that, because it is way bigger than the traditional expenditure, the non-mandatory expenditures. So I think we need to have our budget process look at that side.

I think we also should consider having our budget process look at mandatories, because I do think there are areas in which you can address things without having to create enormous rows. And I will make one proposal. I recall that if you looked at what CMS is obliged to pay per capita State by State and you look at, if my recollection serves, Minnesota and Mississippi, they are paying twice as much per capita in Mississippi as they do in Minnesota. What is going on? Why is it that some States are allowed to run programs that are wildly expensive compared to the norm? And what could we do to make States look more like Minnesota in terms of their per capita expenditure? And maybe if you put a little bit of a belt around the mean so that States that were really grievous outliers on the bad side simply did not get that money, that would focus the mind of those Governors, those State medical associations, those State hospital associations very considerably into how you deliver better care, because I think most people would argue that the care in Minnesota is better than the care in Mis-



issippi; and, indeed, that better care is very often associated with lower cost as a general principle.

So there are areas for looking at where you are not just going in and saying we are going to have to cut that benefit, we are going to have to, you know, do sort of Civil War medicine on the health care programs, when, in fact, just the very ability among the States shows what the room is for improvement on the part of certain States.

And I will close with this comment, which is that if this Committee does not produce something that is bipartisan, then game over. At that point you are just part of the bipartisan fighting here. And that has its role, and I understand that. But one of the things that we stand a possibility of doing is putting something together that has significant bipartisan support in this Committee. And if we do, that will be a very significant set of gravity for the Senate at large. And that is something I think many of us would like to work on.

So, again, I will close by thanking the Chairman for his leadership into this area. I think it is a very wise and good place to be directing our attention in this period of not doing a Budget Committee budget because we do not need to, because we have a budget already agreed to. And I look forward to the very terrific witnesses contributing in writing their thoughts to what I hope will be a meaningful review of how we budget for this great country.

Thank you, sir.

Chairman ENZI. Thank you. And you will be pleased to know that I just asked CRS for an updated tax expenditure report so we would know where they came from, what they do, how much they cost. I had a whole series of questions regarding that, to ask them to update that.

Senator WHITEHOUSE. Yes.

Chairman ENZI. I saw an old list of it, but I have not seen any—

Senator WHITEHOUSE. And, of course, some of it is, you know, pretty good stuff that American families count on, like the home mortgage tax deduction. But some of it smells to high heaven and was snuck in by lobbyists at midnight and has real—I mean, it is the kind of thing that makes people go out and get mad as hell in the voting booth. And we should clean it up. It is a swamp.

Chairman ENZI. So we will not only have to take on the appropriators, we will have to take on the Finance Committee when we start to get into taxes, too.

Senator WHITEHOUSE. That is right.

Chairman ENZI. I look forward to some meaningful discussions with you, and I have some more questions, but I will submit those in writing as well, and I am sure there will be others on the Committee.

Chairman ENZI. There is getting to be more interest in doing this, as they think that maybe it is a possibility. We had a lot more show up today than we have had in the past. But I have been sharing some of the results of what we have come up with before with them.

So with that, I will adjourn the hearing. People can turn in questions until 5 o'clock today. Thank you.

[Whereupon, at 11:48 a.m., the Committee was adjourned.]

Dr. Kevin Hassett  
Director of Economic Policy Studies  
American Enterprise Institute

Responses to Questions for the Record

Senator Ayotte

**Question #1:**

Congress' broken budgeting system, where the authorizing committee is supposed to authorize a program and the appropriating committee is supposed to allocate funding, is broken. Do you think that we can increase certainty and cut down on wasteful spending and duplicative programs by getting rid of the appropriations process all together?

Although this approach would not be popular, it would give the committees that are most knowledgeable the ability to authorize, fund and prioritize programs that are needed.

It is correct that this design is for the most part unique to the U.S. Federal government. It is far more common to combine the two functions into a single committee, and states around the country that do that often function effectively. It would like increase certainty and cut down on wasteful spending if the budget process were transparent, and less likely to run into roadblocks. Whether a reform such as the one you suggest would accomplish that is an open question in my mind. After all, appropriators do not have the best track record when it comes to budget discipline.

**Question #2:**

One of my biggest concerns is Congress' currently inability to complete the budget process on time. Over the past 40 years, we have only completed the budget process on time 4 times – most recently in 1997 – and we have had 173 short-term funding bills.

Since 1996, Congress has completed appropriations measures an average of 104 days after the start of the fiscal year.

In my home state of New Hampshire, we use a biennial budget process. With a national debt over \$18 trillion, it's time to bring New Hampshire common sense to how federal spending decisions are made.

In thinking about budget process reform, do you think it's more appropriate for us to compare biennial budgeting to short-term funding, rather than annual budgeting, since we so rarely complete the budgeting process?

Has the annual budget timeline contributed to dysfunction in the budget process?

**Would moving to biennial budgeting help to resolve these issues?**

**Do you think biennial budgeting would help Congress complete a budget more often?**

Biennial budgeting could possibly increase the urgency that Congress attaches to reaching agreement on a budget. If the biennial budget process always included other possible road blocks such as the debt limit, then the benefits could be significant. The idea that a timely budget could help reduce uncertainty that plagues both government agencies and financial markets is not controversial among economists.

**Question #3:**

**I frequently hear from small businesses in my home state that uncertainty in Washington makes it hard for them to plan and grow.**

**Do you have any recommendations on how we can ensure that Washington provides our job creators a more stable environment?**

Sen. Portman introduced the *End Government Shutdowns Act*, which I cosponsored. The bill is aimed at preventing last-minute budget deals that fail to address our out-of-control spending, as well as aimed at ending the threat to cut off essential federal government services. It creates an automatic continuing resolution (CR) for any regular appropriations bill, lessening the chance of last-minute, budget-busting bills being forced through against the threat of a government shutdown.

**Do you think that this bill could help provide certainty for our job creators?**

I commend you and Senator Portman for your work on this important issue. As I discussed in my testimony, there is ample evidence that uncertainty has a big impact on markets and the economy. While government shutdown threats might seem to have a fleeting impact, the fact that the game of chicken is repeated often is clearly a negative for the U.S. economy. My own view is that the best way to fix the problem is for our elected officials to debate and establish the characteristics of a "reasonable" budget, and for the debt limit and continuing resolutions to automatically follow so long as the budget is "reasonable." For example, we might decide that a budget deficit at or below the long run average is "reasonable."

Senator Enzi

**Question #1:**

Seventy percent of government spending is automatic. Even if Congress does nothing, checks go out the door and spending continues to grow. This automatic spending will bring back trillion-dollar deficits in just 6 years, according to the Congressional Budget Office. These deficits are unsustainable and will bankrupt the country if Congress does nothing.

**What would an enforceable deficit-reduction plan do to increase certainty and stability?**

Long run budget uncertainty is clearly a big negative for the economy. While the literature on the long run positive effects of "fiscal consolidations" is still evolving, there are estimates in the literature that suggest that economic growth would be perhaps as much as 1 percent per year higher if the U.S. could pass a sensible budget reform. My own guess is that the positive effects in the U.S. could be smaller, as we are not experiencing a crisis in confidence in our country along the lines of that facing Greece, but that the effects would nonetheless be quite positive. I should also add that uncertainty also has a negative effect on individuals who benefit from our entitlement programs. If your Social Security payments go down surprisingly when you retire, then you will be much worse off than you would have been if you had ample time to plan and save for a retired life with lower benefits.

**Question #2:**

The budgets produced by the House and Senate budget committees lay out long-term fiscal strategies, but they bear little relation to the eventual tax and spending decisions enacted by Congress.

**How successful is the current process at governing future budget decisions and enforcing fiscal discipline? How important is it that the budget resolution act as a governing plan?**

The current process is completely broken. The House and the Senate promise to be virtuous in the future, and regularly renege. A budget resolution that provides multi year clarity, and a budget process that charts a course that is free from cliffs and roadblocks could significantly reduce harmful uncertainty.

**Question #3:**

The debt limit is a significant source of uncertainty when it is used as leverage during budget negotiations, but it is also an important reminder that Congress's decisions to spend more money have consequences.

**How could we reform the debt limit so that it is incorporated into Congress's tax and spending decisions but cannot be used to force unnecessary crises that rattle financial markets?**

As mentioned in my testimony, and in answer to Senator Ayotte, I believe that we should establish the characteristics of a reasonable budget, and that the debt limit should be lifted automatically for any budget that meets the characteristics. For me, one simple metric might be to consider a budget reasonable if it calls for a deficit that is at or below the long run average.

#### Senator Kaine

##### Background:

The federal government lacks a debt management policy that are commonly used by states and localities manage debt. Right now, the debt ceiling is a forcing mechanism, but its focus on debt as a dollar amount, or as a date up until which the federal government may borrow, fails to accurately capture the size of our economy, or changes in the economy. Despite the fact that states and localities differ in some ways in budgeting needs from the federal government, I believe we should address the government's debt management policy.

Congress should do more to focus on debt ratios - such as debt as a percent of gross domestic product (GDP) and/or debt service as a percent of the annual federal spending. This would be a better way to analyze spending, revenues, deficits, and debt. It would also provide more certainty to government employees, contractors, families, states and localities, and the private sector.

##### Question:

**Do you believe Congress could establish an improved federal debt management policy? In your view, what would such a policy look like, how would it be achieved, and what positive outcomes could it generate? What obstacles would there be to establishing such a policy, and how could we overcome them?**

I commend your focus on ratios. For the most part, the economic literature that analyzes the impact of debt and deficits on economic activity does so by relating economic growth to the ratio of these to GDP. We know where the danger zones are, and the current process obscures them.

I favor a policy that ensures that the government functions smoothly, for example, that lifts the debt limit, so long as a budget is "reasonable." The metric of "reasonable" is worthy of a number of hearings, but a simple one might be that the deficit relative to GDP is at or below its

long run average. Many may favor additional conditions related to spending relative to GDP, and tax revenue relative to GDP. Such a measure could eliminate the negative short run uncertainty highlighted in my testimony.

Many countries around the world have established targets such as the ones I mentioned. A major concern drafters of the legislation should have is what we should do during recessions. My own view is that deficits increase in recessions, so budget rules should be relaxed. The problem is, however, that recessions are often declared by the NBER after they are over, as economic data come in with a lag. Accordingly, it might be that the rule could be suspended when the BEA's GDP estimate is below zero for two consecutive quarters.

#### Senator Perdue

##### Question #1:

**Currently we have a funding cycle that starts with a budget resolution, followed by reauthorization of spending, and finally appropriations. In the past decade, we've failed to pass a budget resolution more often than we have passed one, outside of NDAA, we have failed to reauthorize programs in an orderly fashion, and in the past 40 years, we've only appropriated according to plan 4 times. In a white board approach, if the goal is to fund the government and review its operations, how would you recreate the budget, reauthorization, and appropriations process in the Senate? Would you consolidate steps in the process? Would you redesign the process to include all revenue and outlays?**

While I am sympathetic to ideas that may streamline the process by consolidating steps, my own view is that the major obstacle has been the budget resolution. I believe that a reform that establishes characteristics of a "reasonable" budget resolution, and eliminates road blocks if a budget is passed that is reasonable could create an environment that significantly improves the budget process and rewards responsible and timely budgeting. My own metric of "reasonable" would include a deficit target relative to GDP. It might be that others would like to include spending and tax targets. It would also be natural to expect a reasonable budget to be passed early in a legislative cycle, so that it could provide guidance to the appropriate committees and subcommittees. I agree that major surgery for the entire process could be successful, but this simple high-level reform could well have a major impact, and is worth trying first.

**Responses to Questions for the Record**

**“Tap Dancing on the Razor’s Edge: Restoring Stability to Government Operations”**

**Senate Budget Committee**

**April 20, 2016**

**Dr. Philip G. Joyce**

**University of Maryland School of Public Policy**

**Senator Kaine**

**Question:**

The federal government lacks a debt management policy that are commonly used by states and localities manage debt. Right now, the debt ceiling is a forcing mechanism, but its focus on debt as a dollar amount, or as a date up until which the federal government may borrow, fails to accurately capture the size of our economy, or changes in the economy. Despite the fact that states and localities differ in some ways in budgeting needs from the federal government, I believe we should address the government’s debt management policy.

Do you believe Congress could establish an improved federal debt management policy? In your view, what would such a policy look like, how would it be achieved, and what positive outcomes could it generate? What obstacles would there be to establishing such a policy, and how could we overcome them?

**Response:**

As someone who has worked in a state budget office, advised a local school board, and worked for the federal government, I share your concern that the federal government has no reliable way to control its debt. This is a complicated issue, so I would like to make several points related to this.

1. Virginia, with its well-earned AAA rating, and other states do manage debt, but they do so partially because of the “unseen hand” of the bond rating agencies. When states acquire too much debt, they risk a downgrade, which has budgetary (higher interest rates), economic, and political fallout. There is no such incentive for the federal government. Federal debt went from about 50% of GDP to 80% of GDP after the Great Recession, and interest rates went DOWN.



2. Part of this is because the federal government has countercyclical responsibilities that states and local governments do not have. Generally, we want the federal government to provide economic stimulus during a recession, but this responsibility drives up debt. In fact it was actions of the federal government, in part, that kept states and localities from having to take more draconian actions during the recession. There is no reason, however, for the debt to remain at that high level when the economy moves out of recession.
3. State and local governments, as you said in the hearing, borrow for capital purposes, which at least constrains the purpose of borrowing to the kinds of expenditures that may tend to yield long-term benefits. The federal government borrow indiscriminately, since borrowing is the just done to finance the difference between taxes and spending.
4. Having said this, however, what the federal government lacks is what many other countries describe as a “fiscal rule”. A fiscal rule could be as simple as a balanced budget requirement, although I am not a supporter of that kind of rule for the federal government. Many countries establish a fiscal rule in law that normally represents some ratio of debt to GDP. This is very similar to what I am sure you experienced in Virginia, since many states and localities establish ratios (debt/personal income, debt service/revenue, per capita debt) that drives their practices on the accumulation of further debt. I would support the passage of legislation that defined a fiscal rule for the federal government. I would think the first step would be to establish a path and timetable for debt reduction (as in, reduce the debt to no more than 60 percent of GDP by 2025). I think the lack of consensus on a fiscal goal is the biggest obstacle to a more fiscally responsible budget policy.
5. Having a fiscal rule would tell you where you want to go, but would not tell you how to get there. So I would say the biggest obstacle would be in converting the goal established in the rule to the policies that would be necessary to reach the goal. In a sense that is the problem that you already have, except that at present there is no consensus on the overall goal for fiscal policy.

**Responses to Questions for the Record**

**“Tap Dancing on the Razor’s Edge: Restoring Stability to Government Operations”**

**Senate Budget Committee**

**April 20, 2016**

**Dr. Philip G. Joyce**

**University of Maryland School of Public Policy**

**Chairman Enzi**

Question:

Congressional budget decisions are made by authorizing committees that enact mandatory spending, appropriators that enact discretionary spending, and the Finance Committee that considers changes to the tax code. This is a very fragmented process.

The budget committees are tasked with publishing a unifying plan that allows Congress to consider all areas of the federal budget together. However, their influence has varied over the last 40 years.

How would you strengthen the budget committees so that the decisions made in the budget would influence and govern the tax and spending decisions made by Congress?

Response:

The 1974 Congressional Budget Act created the Budget Committees as the only committee with responsibility for the big picture. Because the other fiscal power centers (appropriations and tax writing committees) did not want the Budget Committees to be more powerful, they intentionally placed checks on their power (having them focus on “functions”, for example, that are not directly related to committee jurisdictions).

Not only because of institutional weakness, but also because of choices made by the Congress to not adopt a budget resolution, the budget resolution process has become dysfunctional. The budget resolution itself has become a hit-and-miss affair, and reconciliation is as likely to be used to make deficits larger as it is to promote fiscal discipline.

The Budget Committees are the only committees charged with taking an overall view of the budget, and thus are uniquely positioned to assist the Congress—and the country—in addressing a multi-year budget problem. The budget resolution—especially because of reconciliation—is the only multi-year budget device that the Congress has at its disposal. Therefore, current challenges suggest that strong consideration should be given to making the Budget Committees

stronger. I would do this by renaming the budget committees as “Committees on National Priorities” consistent with a proposal made by Senator Kassebaum in the 1980s and 1990s. The revised committees would include chairs and ranking member of appropriations, tax committees, and other authorizing committees, as well as representatives of the leadership.

Such a reform would likely make it more likely that a budget resolution would be adopted, since failure would be seen as a specific failure of the leadership. Other committees, since their chairs and ranking members would be on the new committees on national priorities, would be less likely than they are at present to attempt to undermine the policies reflected in the budget resolution.

## Responses to Questions for the Record

## "Tap Dancing on the Razor's Edge: Restoring Stability to Government Operations"

Senate Budget Committee

April 20, 2016

Dr. Norman Ornstein

American Enterprise Institute

Senator Kaine

Question:

The federal government lacks a debt management policy that are commonly used by states and localities manage debt. Right now, the debt ceiling is a forcing mechanism, but its focus on debt as a dollar amount, or as a date up until which the federal government may borrow, fails to accurately capture the size of our economy, or changes in the economy. Despite the fact that states and localities differ in some ways in budgeting needs from the federal government, I believe we should address the government's debt management policy.

Do you believe Congress could establish an improved federal debt management policy? In your view, what would such a policy look like, how would it be achieved, and what positive outcomes could it generate? What obstacles would there be to establishing such a policy, and how could we overcome them?

Response:

Finding a reasonable debt management policy is a laudable goal for the federal government. But I am hesitant to endorse a specific plan. The federal government is not the same as states; it has different responsibilities and functions. That is why I believe it would be catastrophic to enact a constitutional amendment to balance the budget. When we hit a serious economic recession or downturn, most states must cut spending and/or raise taxes to balance their budgets and conform to their debt management criteria. If the federal government did so at the same time, it would be the equivalent of bleeding a medieval patient to death—we need countercyclical stimulus from the federal government to keep the economy under those conditions from sinking much further.

To be sure, balancing a budget is not the same as managing debt. But any mechanism that is forcing—requiring the government to spend less when it hits some threshold, even when it may involve financing a war or coping with a massive natural disaster—is perilous at the federal level. And, as we have seen with the manipulation for political and radical ideological purposes of the debt ceiling, it can become an instrument of blackmail.

Having said that, if Congress had an automatic and meaningful pay as you go provision—including revenues with spending as options—that was triggered whenever the debt to GDP ratio hit a certain

percentage (and with an out for traumatic economic times, like the financial and economic collapse in 2008) I would be supportive.

**Senator Stabenow**

**Question #1**

The budget drama of the past several years has inflicted widespread damage on American families and businesses. Unfortunately Congress hasn't only subjected Americans to budget uncertainty and continuing resolutions. Partisan budget brinksmanship intended to extract political wins has nearly sent the country into default and has caused government shutdowns.

The use of these tactics has increased over the last several years, despite solid evidence on the damage they cause. In 2011, debt ceiling brinksmanship led to the first ever downgrade in the Standard & Poor's credit rating of long-term federal debt. The delay in raising the limit led to a \$1.3 billion increase in the Treasury's borrowing costs, and according to the Bipartisan Policy Center, the political showdown cost taxpayers \$18.9 billion over 10 years.

Despite this, last year, some members of Congress again threatened an unprecedented default. The shutdown threats and actual shutdowns are just as damaging. The 2013 shutdown led to \$24 billion in lost economic growth.

Dr. Ornstein, do you agree that the problem of budget brinksmanship has been getting worse, and if so, why?

**Response:**

There is no doubt the use of budget weapons as hostages and as tools to accomplish either extraneous goals or to hamper government functions has been growing, especially during the Obama years. While the debt ceiling has been a political instrument and political football for decades, used by both parties when the other side occupied the White House to demonstrate fiscal fealty, it was long understood that the political games would be limited—that if the risk of a default or breach in the debt limit were real, the votes would be rounded up to avoid catastrophe. That has not been true in the same way since 2009. Congressman Jason Chaffetz openly bragged that he and his colleagues were ready to take it over the cliff, and the use of the debt ceiling as a hostage was openly celebrated by Senate Republican Leader Mitch McConnell.

Add to the debt ceiling confrontations, the threats, and then reality, of government shutdowns, which disrupt fundamental government services, damage our government workers, and can create upheaval among taxpayers and their families. These threats, too, have grown in recent years and loom again in 2016. As I testified, end game negotiations, and brinksmanship, are standard when it comes to important decisions that shape our policy. There is nothing new about budget and spending deals happening at the last minute. But when a substantial group of members see a shutdown as a goal in and of itself, it is time to worry.

**Question #2:**

The cost of the recent budget drama goes beyond the immediate damage caused by shutdowns, continuing resolutions, and near-breaches of the debt ceiling. I believe the other budget crisis is the failure to adequately invest in the types of things we already know grow our economy, prepare our workforce, rebuild the middle class, and ultimately improve the nation's budget outlook. Passing a continuing resolution, while certainly better than a shutdown, doesn't address our changing long-term funding needs.

For example, our infrastructure is in desperate need of investment to keep the economy moving. According to the American Society for Civil Engineers our infrastructure is rated D+ and will need \$3.6 trillion of investment by 2020 just to get a grade of B. This investment isn't optional. Just ask the people of Flint Michigan, who know more than most about the impacts of a failing water infrastructure. And across the country, another 2,000 water systems have shown excessive levels of lead in the past four years.

Budget brinksmanship has at its best resulted in status quo and at its worst, under sequestration brinksmanship results in across the board cuts that we thought would be too damaging to ever actually occur. Dr. Joyce and Dr. Ornstein, you both note that dysfunction and uncertainty often mean that important investments are not made, which can lead to higher future costs.

Can you elaborate on the costs of failing to invest in programs with known long-term benefits? What examples have you seen of mindless budget austerity programs such as sequestration leading to problematic disinvestment?

**Response:**

In the largest sense, it is the inability to implement sensible public policy even when there is some measure of bipartisan consensus that is most troubling about our current dynamic. No area is more emblematic than infrastructure. The needs, both to modernize crumbling sewer and water lines, locks and dams, roads and mass transit, and to make safe and efficient energy operations, including the electrical grid, while using new technologies to make American more competitive, are deep and obvious. And the ability to pay for it with very low interest, long term infrastructure bonds, makes it a win/win/win. Infrastructure, medical and energy research and development, education and training, are all areas where government spending is an investment, not simply transferring money from one person, group or institution to another. And we know the payoffs of such investments, as in, for example, research on Alzheimers disease, can reduce both pain and immense expense down the road. A myopic view of government, and the idea that disrupting programs and cutting spending are the only meaningful goals, undermines the future of our society.

**Senator Perdue****Question:**

Currently we have a funding cycle that starts with a budget resolution, followed by reauthorization of spending, and finally appropriations. In the past decade, we've failed to pass a budget resolution more often than we have passed one, outside of NDAA, we have failed to reauthorize programs in an orderly

fashion, and in the past 40 years, we've only appropriated according to plan 4 times. In a whiteboard approach, if the goal is to fund the government and review its operations, how would you recreate the budget, reauthorization, and appropriations process in the Senate? Would you consolidate steps in the process? Would you redesign the process to include all revenue and outlays?

**Response:**

This is a hugely important question. I do believe that we have at least one too many separate layers in Congress, including budget, appropriations, authorizations and taxation. I understand the reason why Congress originally separated out appropriations from authorization, to provide a meaningful check on government (the idea was appropriators would be more stringent with taxpayer dollars, not so captured by the programs' interests) and additional, separate eyes for oversight. But it is clear this process has not been working for some time. Oversight has largely been lost or seriously reduced. The authorization process is a joke—programs have gone for years and decades without the supposedly required reauthorization. I would probably merge the two functions together, with a dozen committees each taking on a set of programs and agencies, and doing both authorizing and appropriating. Having a panel that looks at the larger picture makes sense. But as a thought experiment, how about also merging the budget-setting and taxing functions? Set the overall number—and a revenue amount that fits.





## BETTER BUDGETS, BETTER RESULTS

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WEDNESDAY, APRIL 27, 2016

U.S. SENATE,  
COMMITTEE ON THE BUDGET,  
*Washington, D.C.*

The Committee met, pursuant to notice, at 10:32 a.m., in Room SD-608, Dirksen Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Crapo, Ayotte, and Whitehouse.

Staff Present: Eric Ueland, Republican Staff Director; George Everly, Chief Counsel; for the Minority: Joshua Smith, Budget Policy Director.

### OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. Good morning. I will go ahead and call to order this meeting of the Senate Budget Committee and welcome everyone to the fourth hearing in a series the Committee is holding to fix America's broken budget process.

The Democrats are having a caucus, as I understand it, right now. I imagine it might have something to do with the appropriations bill that we are doing right now. But as soon as Senator Whitehouse shows up, we will have him give his opening statement. But we will go ahead and proceed because we have a noon vote today to work in as well.

Over the hearing arc, we are beginning to see increasing support and acknowledgment from both sides of the aisle that our budget process is broken, and now is the time to fix it. Instead of the current budget process, which is designed to fail both Congress and our constituents, it is time to put forth a budget process that is designed to succeed. Our spending decisions are fragmented across multiple committees and Federal agencies. Dysfunctional annual appropriations create uncertainty that negatively affects agencies, businesses, and individuals. And mandatory spending is literally surging out of control, driving future deficits and debt to unsustainable levels.

Congress also fails to review its past spending decisions and results after the funds have been spent. GAO's Comptroller General told us that his agency is unable to properly audit the Government because it cannot keep track of all of the assets and because of different definitions between agencies. This means Congress does not know whether previous Federal spending has been effective because program performance data is completely disconnected from

congressional spending decisions, and good performance is not rewarded and bad performance has no consequences.

And it is clear from our previous hearings that even if we have not yet agreed on a particular path forward, we all agree that something must be done. There have been many good ideas presented on how to fix the process. We have heard big, comprehensive ideas that fundamentally change the way Congress and the executive branch of Government allocate resources. And we have heard more narrow and targeted ideas that could at least begin to improve the current process.

Today we will hear more reform thoughts from our panel of experts. This hearing is critically important because it focuses on the actual budget documents created during the annual budget process. The President's budget submission and the congressional budget resolution are supposed to serve as unifying documents that set forth serious, comprehensive fiscal plans for the Government. But both have become increasingly meaningless as tools to govern and bear little relation to the actual tax and spending decisions made by Congress.

The President's budget is a massive undertaking that consumes over 2,600 pages. While some of the information provided is useful, many of those pages are full of spin, talking points, and proposals that everyone knows are dead on arrival. The document is so huge that it limits its usefulness. In many ways, this document has become, through several administrations, a giant press release focused on messaging rather than as a serious plan to address the challenges facing the state of our Union.

The statutes governing the content and structure of the President's budget result from a patchwork of legislation pieced together over the past century. And the current format of the President's budget is largely based on a plan developed in 1912 during the Taft administration. The structure of the President's budget was not planned but evolved, and no matter how far it has evolved, one thing is clear: This document is not 21st century budgeting.

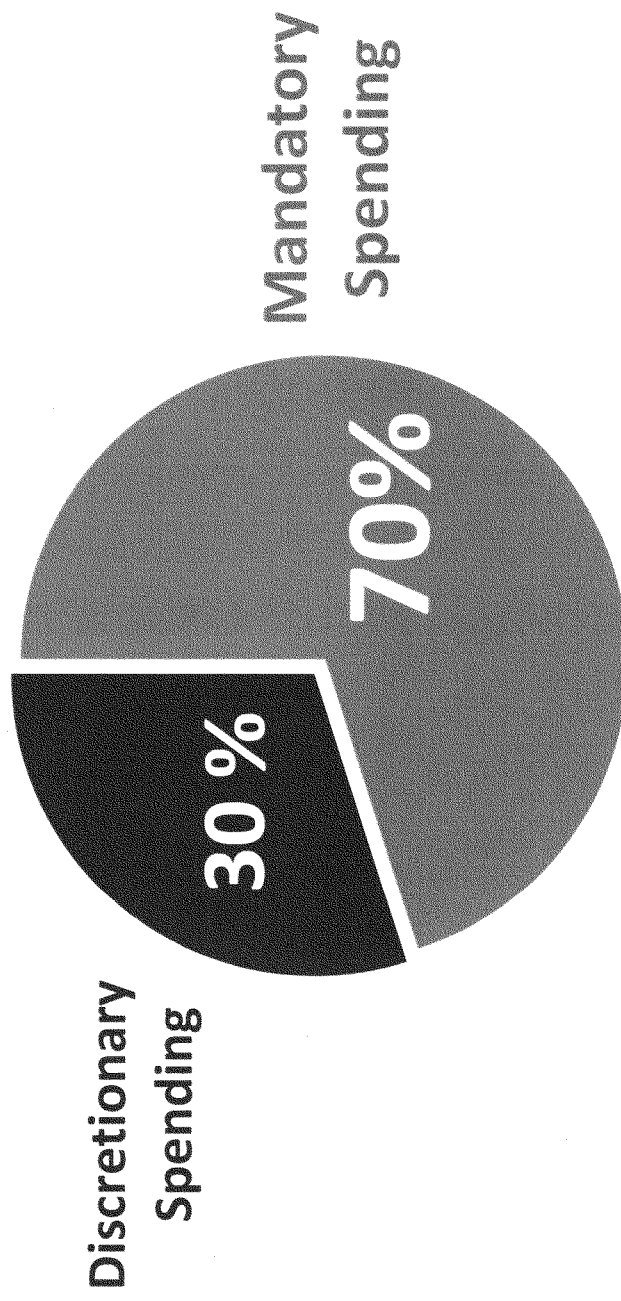
The President must have a more constructive role in the budget process. If not, his only recourse is to veto large tax and spending bills, creating showdowns, shutdowns, and crisis deals negotiated behind closed doors, usually after the fiscal year starts. This undermines the fiscal discipline and financial future of our Nation. Involving the President early in the negotiating process will allow Congress to develop a clear path forward for budgeting and passing over regulation and legislation.

My concerns are not just with the President's budget. The congressional budget resolution has also been similarly irrelevant. In theory, it should serve as a fiscal blueprint that coordinates revenues and spending and that connects congressional priorities with committee legislation. And it is the only tool that Congress has to control runaway mandatory spending.

As you can see in the chart on the screen, this portion of the budget has grown to 70 percent and will bankrupt the country if nothing is done. It is not working. Seventy percent of Government spending is not regularly reviewed by Congress, and that does not include expired programs we still fund. In practice, its limits on discretionary spending have been superseded by statutory caps,

and its limits on mandatory spending are routinely ignored or put aside because it only takes 60 votes—the same amount required to end debate on legislation.

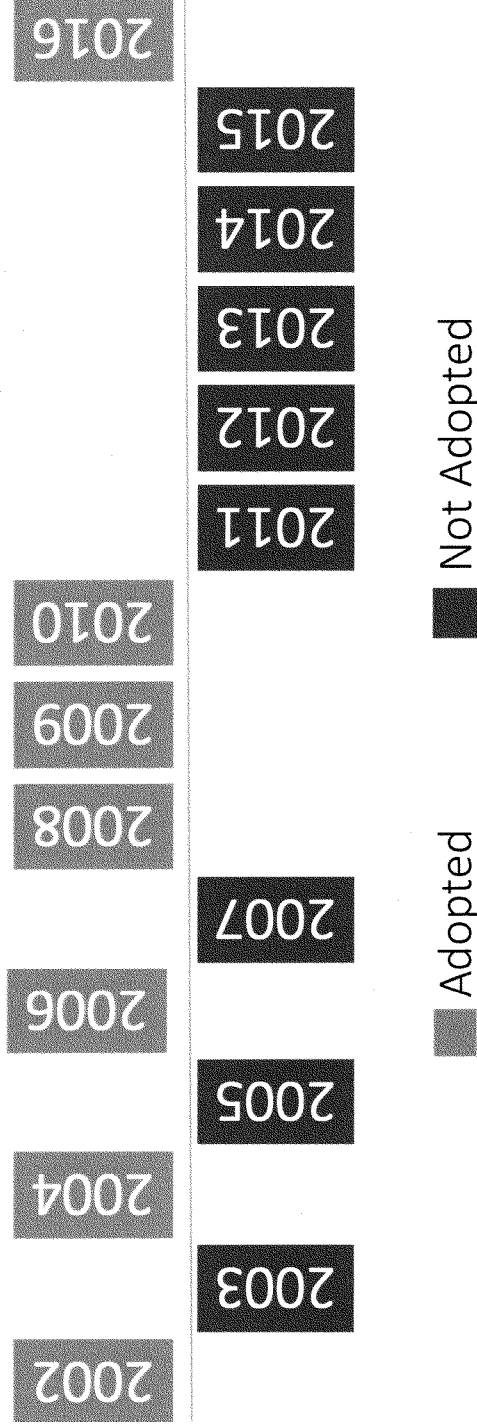
## Seventy Percent of Government Spending Is Not Regularly Reviewed by Congress.



One of Washington's dirty little secrets is that the amount our Government spends in a given year almost never matches the amount the budget resolution contains. But even that "let us pretend" process is falling apart.

In the last 15 fiscal years, Congress failed to pass a budget resolution more than half of the time, as shown in this graphic. Prior to 1997, it had never failed to pass a budget. The congressional budget should provide predictability and certainty, the limits it establishes should be enforceable, and the tax and spending measures Congress passes should adhere to the budget.

# Congress Adopted Only 7 Budgets in Previous 15 Fiscal Years



The Federal Government's budget should be a long-term, enforceable plan that provides predictability, transparency, and accountability. Members of this Committee know that our current process by design fails to do that. No one can guarantee which party will win the Presidency this fall or who will be in the majority. We all know that voters have a way of upending expectations.

So now we have a unique opportunity—and it probably will not happen again for another 4 years—to fix America's broken budget process so that it can matter once again. I especially appreciate the willingness of my colleagues to engage in a constructive and bipartisan manner on one of the most important and serious challenges facing this country. And I have appreciated the ideas from both sides of the aisle that have been put forward on this, many of which I think can be included in a document.

So I look forward to a positive and elevated conversation with our witnesses today which matches the seriousness of the purpose to which we are engaged.

Since Senator Whitehouse is not here yet, I will go ahead and introduce the witnesses and I thank our witnesses for being here today. The tradition in all of the committees, of course, is that people that are not there, and even ones who are there, can submit questions up until 5 o'clock today, which we hope you will also respond to. Often what is in writing is more helpful because it is more detailed usually than what we cover in the public part of the hearing.

Mr. Barry Anderson has extensive experience dealing with Federal budgeting in the United States Federal Government as a senior career official at the Office of Management and Budget and as the Deputy Director and then the Acting Director of the Congressional Budget Office. He was on both sides. He also has experience dealing with the budgets of other nations. Mr. Anderson has been the head of the Budgeting and Public Expenditures Division in the Organization for Economic Cooperation and Development, OECD, in Paris. He has also served as a budget adviser at the International Monetary Fund. And, finally, he has served as the Deputy Director of the National Governors Association.

Mr. James C. Capretta is a Mercatus Center Affiliated Scholar, a senior fellow at the Ethics and Public Policy Center, and a visiting fellow at the American Enterprise Institute. He has served in senior positions in the executive and legislative branches of the Federal Government for 16 years. He previously worked at OMB and on the staff of the Senate Budget Committee and on the staff of the House Ways and Means Committee.

Our third witness, Mr. Stanley Collender, currently serves as the executive vice president of communications at Qorvis. Mr. Collender has worked for three Members of the U.S. House of Representatives and on the staff of the House Ways and Means Committee and on the staff of both the House and Senate Budget Committees. As a member of the House Budget Committee staff, he served as administrator of the Task Force on State and Local Government. For the Senate Budget Committee, he was responsible for analyzing defense spending. He is also the author of "Capital Gains and Games," a blog published by Forbes.

So I want to thank all three of you for joining us today to share your expertise, and I appreciate the written testimony that you have already provided. The entire testimony will be a part of the record.

So, with that, we will go ahead and get the testimony. I will begin with Mr. Anderson.

**STATEMENT OF BARRY ANDERSON, FORMER ACTING DIRECTOR, CONGRESSIONAL BUDGET OFFICE, AND FORMER SENIOR CAREER OFFICIAL, OFFICE OF MANAGEMENT AND BUDGET**

Mr. ANDERSON. Thank you, Chairman Enzi, and to the members of the Committee for the opportunity to appear before you to discuss proposals to reform the President's and congressional budgets.

As you have mentioned, Chairman Enzi, I have had a very long career in budgeting—30 years at the Federal level at OMB, CBO, and GAO; 5 years at the international level at the OECD in Paris; 5 years at the State level at the National Governors Association; and 2 years at what I call the “supra-national level” at the International Monetary Fund.

Over the years, I have seen budgeting from many perspectives, and believe it or not, I think that the foundations of our Federal budget system are sound. These foundations include: the separation of powers; the use of obligational (as opposed to cash or accrual) budgeting; generally transparent information on revenues (including tax expenditures), on credit programs, on performance assessments; even on our elaborate budgetary enforcement mechanisms such as the Anti-Deficiency Act and sequestration. That said, there is undoubtedly much room for improvement.

But my testimony today concerns only one aspect of our Federal budgetary system: proposals to reform the President's budget. I have three recommendations focused on changes that would make the President's budget more relevant to the process of setting a Federal budget:

Number one, bring back the Citizen's Guide to the Federal Budget. The latest President's budget—the fiscal year 2017 budget—has seven different documents totaling over 2,600 pages. “Spin”—or the political promotion of the President's proposals—is everywhere. Perhaps that is to be expected. It is, after all, the President's budget proposals. But for many years previous Presidents also submitted a short—30 pages or so—easy-to-read, fundamentally factual description of the Federal Government's fiscal status that was originally called “The Budget in Brief” but in the 1990's was renamed “A Citizen's Guide to the Federal Budget.” Sure, it contained a summary of the President's proposals, but the summary was only a few pages, not several hundred. By making the increasingly complex budget easier to understand, the Citizen's Guide helped the public, the press, and politicians frame their views on the difficult budgetary decisions that must be made every year. In other words, it made the President's budget more relevant to the larger budgetary process.

The acceptance of a budget's proposals varies from President to President and from year to year, but whatever the reaction to the President's budget, the Citizen's Guide in the past has helped both



the opponents and proponents of the President's proposals understand the country's current and projected fiscal status, and by so doing the reasons behind the President's proposals, whether they agreed with them or not. Bringing back the Citizen's Guide is in no way a solution to the fundamental political differences that currently divide our country, but a factual presentation that helps the public, the press, and politicians understand the President's proposals as well as the country's underlying fiscal status can surely help bridge our differences and make the President's budget more relevant.

Number two, emphasize long-term budget projections. The current fiscal status of the United States Government is not the fiscal problem of greatest concern. Projections of our fiscal status over the long term is. Capital markets, both domestic and international, are currently providing the money we need to finance our ever-growing debt at low interest rates, and despite near universal recognition that our deficits and debt will continue to grow, the difficult status of other international borrowers and the level of savings looking for "safe" investments as the world ages mean that we can probably continue to finance our growing debt at relatively low INT rates in the near future.

But our population is also aging rapidly, and baby boomers like myself are retiring in the thousands every month. These demographic pressures coupled with generous programs for the elderly, infrastructure needs, man-made and natural disaster risks, and the public's natural reluctance to support tax increases result in a very grim fiscal future indeed. Yet despite the widespread recognition of this grim forecast and despite the widespread recognition that certain actions taken today can significantly improve our long-term fiscal future, the fiscal year 2017 budget does not provide a discussion of the long-term fiscal budget outlook until well into the 418-page Analytical Perspectives document.

The importance and impact of today's policies over the long term demands that long-term projections be made an integral part of the President's budget. Long-term projections under current policies and how those projections might change under the President's proposals should be displayed and discussed along with short- and medium-term projections.

Recognizing that the longer the projections, the more uncertainty is involved means that it is even more important to be fully transparent about the assumptions behind the projections as well as to display the sensitivity analysis about the major factors that influence the projections. Despite these uncertainties, it is far superior to display and discuss the potential long-term fiscal impacts of the President's budget proposals than to pretend that they do not exist by ignoring them. In sum, the President's main budget document should display and discuss the potential impacts of its policy proposals on its long-term projections in the same manner that it displays and discusses the potential impacts of policy proposals on short- and medium term projections, not hide them in some technical document.

Number three, revise the content and presentation of the President's budget documents. I have mentioned above that bringing back the Citizen's Guide would help increase the relevance of the

President's budget. And revising the content and presentation of the remaining budget documents could also help. Let me mention the four main major documents.

The Main Budget Document, which is about 200 pages. The President presents his budget proposals in this document, and it should remain the primary place for political arguments supporting the President's proposals. Adding long-term projections to the document and, perhaps, some of the political chapters currently in the Analytical Perspectives, which I will mention next, are the only changes I would make to this document.

Next is the Analytical Perspectives Document, which is about 400 pages. Years ago, this was called "special analyses," and then it was condensed into the Analytical Perspectives document, and it was solely a technical document. It should be brought back to that. It now has technical presentations on economic assumptions, on Federal borrowing and debt, and on tax expenditures. But in the last couple of years, presentations that belong in the Main Budget document have been added. These include strengthening the Federal workforce and Federal budget exposure to climate risk. Incorporating these political presentations into the Main Budget document—if the President deems them to be important—would cut the size of the Analytical Perspectives by roughly a quarter and make both documents more focused.

The third is the Historical Tables, about 400 pages. During my long career at OMB, I frequently heard that this was the most useful budget document—a true reference source of valuable data available nowhere else. So why is it now available only online? The printed version should be restored immediately.

Lastly is the Appendix Document, about 1,400 pages. This document is prepared primarily for the Appropriations Committees. They need it, and OMB and the agencies need to prepare it to make sure that the budget numbers are both comprehensive and internally consistent, but there is no need to print it for anyone other than the Appropriations Committees.

With respect to these changes, I recommend that a better way than putting them in legislation is to use the confirmation process, Mr. Chairman, for the OMB Director. Getting the agreement of the President's nominee for OMB Director during the confirmation process can provide a personal commitment that members can cite if the changes are not made.

If I can close with one last point, it is time for a new budget concepts commission as former CBO Director Rudy Penner and I wrote last January. The basic concepts underlying the U.S. Government's budget are in disarray. Consider that there is no generally accepted practice about how to deal with such things as what the budget should include, how spending and revenues are defined, or how the budget should be displayed to show the economic impact of different kinds of spending.

The 1967 Report of the President's Commission on Budget Concepts addressed some of these issues and led to some reforms, such as the unified budget. But many issues remain to be resolved, and it is time to create a new commission to address some of these, including:

The scope of the budget. Some programs are on budget, some programs are off budget. Moreover, the way the budget should treat Government-sponsored enterprises and other Government-private partnerships needs to be detailed.

Defining spending and revenues. The distinction between taxes and spending has become muddled and needs to be addressed. For example, "tax expenditures" and "offsetting collections" should to be defined more precisely and their placement in the budget reconsidered.

Thirdly, the economic impact of different types of spending. A new commission needs to recommend better ways of showing the impact of such things as Government purchases of securities, trust funds, capital investments, and loans or guarantees.

Although the topic of budget concepts may seem dry and technical to most Americans, and even lawmakers, almost all of these issues are important economically and have an important political dimension. How the budget is organized and its components defined and represented gives a particular impression about how much money the Government raises and spends and what it does with the money. So clarifying the way the budget is arranged and defining budget terms has important implications. I urge the Committee to work with the President to form a new Budget Concepts Commission.

With that, Mr. Chairman, I would be happy to answer any questions members of the Committee might have.

[The prepared statement of Mr. Anderson follows:]

Statement Before the  
Committee on the Budget  
United States Senate

**Barry Anderson**  
Independent Budget Consultant  
April 27, 2016

Thank you, Chairman Enzi, and the members of the Committee for the opportunity to appear before you to discuss proposals to reform the president's and congressional budgets.

I have had a long career in budgeting:

- 30 years in budgeting at the *federal level*—as the senior career official at the Office of Management and Budget (OMB); as the Deputy and Acting Director of the Congressional Budget Office (CBO); and at the General Accounting Office;
- 5 years in budgeting at the *international level*—as the Head of the Budgeting and Public Expenditures Division of the Organization for Economic Cooperation and Development in Paris;
- 5 years in budgeting at the *state level*—as the Deputy Director of the National Governors Association; and,
- 2 years in budgeting at the *supra-national level*—as a budgetary expert at the International Monetary Fund.

Over the years, I have seen budgeting from many perspectives, and believe it or not, I think the foundations of our federal budget system are sound. These foundations include: separation of powers; use of obligational (as opposed to cash or accrual) budgeting; generally transparent information on revenues (including tax expenditures), credit programs, and performance assessments; even our elaborate budgetary enforcement mechanisms such as the Anti-Deficiency Act and sequestration. That said, there is undoubtedly much room for improvement.

But my testimony today concerns only one aspect of our federal budgetary system: proposals to reform the president's budget. I have three recommendations focused on changes that would make the president's budget more relevant to the process of setting a federal budget:

1. **Bring back the Citizen's Guide to the Federal Budget.** The latest president's budget—the FY2017 Budget—has seven different documents totaling over 2,600 pages. “Spin”—or the political promotion of the president's proposals—is everywhere. Perhaps that is to be expected—it is, after all, *the president's* budget proposals—but for many years previous presidents also submitted a short (30 pages, give or take), easy-to-read, fundamentally factual description of the federal government's fiscal status that was originally called “The Budget in Brief” but in the 1990's was renamed “A Citizen's Guide to the Federal Budget”. Sure it contained a summary of the president's proposals, but the summary was only a few pages, not several hundred. By making the increasingly-complex budget easier to understand, the Citizen's Guide helped the public, the press, and politicians frame their views on the difficult budgetary decisions that must be made every year: in other words, it made the president's budget more relevant to the larger budgetary process.

The acceptance of a budget's proposals varies from president to president and from year to year, but whatever the reaction to the president's budget the Citizen's Guide in the past has helped both the opponents and proponents of the president's proposals understand the country's current and projected fiscal status, and by so doing the reasons behind the president's proposals, whether they agreed with them or not. Bringing back the Citizen's Guide is in no way a solution to the fundamental political differences that currently divide our country, but a factual presentation that helps the public, the press, and politicians understand the president's proposals as well as the country's underlying fiscal status can surely help bridge our differences and make the president's budget more relevant.

2. **Emphasize long-term budget projections.** The current fiscal status of the United States Government isn't the fiscal problem of greatest concern: *projections* of our fiscal status over the long-term is. Capital markets, both domestic and international, are currently providing the money we need to finance our ever-growing debt at low interest rates, and despite near-universal recognition that our deficits and debt will continue to grow, the difficult status of other international borrowers and the level of savings looking for “safe” investments as the world ages mean that we can probably continue to finance our growing debt at relatively low rates in the near future.

But our population is also aging rapidly, and baby boomers like myself are retiring in the thousands every month. These demographic pressures coupled with generous programs for the elderly, infrastructure needs, man-made and natural disaster risks, and the public's natural reluctance to support tax increases result in a very grim fiscal future indeed. Yet despite the wide spread recognition of this grim forecast, and despite the wide spread recognition that certain actions taken today can significantly improve our

long-term fiscal future, the FY2017 Budget doesn't provide a discussion of the long-term budget outlook until well into the 418-page Analytical Perspectives document.

The importance and impact of today's policies over the long term demands that long-term projections be made an integral part of the president's budget. Long-term projections under current policies and how those projections might change under the president's proposals should be displayed and discussed along with short- and medium-term projections under current policies and how they might change under the president's proposals, not relegated to just the technical Analytical Perspectives document.

Recognizing that the longer the projections, the more uncertainty is involved means that it is even more important to be fully transparent about the assumptions behind the projections as well as to display sensitivity analyses about the major factors that influence the projections. Despite these uncertainties, it is far superior to display and discuss the potential long-term fiscal impacts of the president's budget proposals than to pretend that they don't exist by ignoring them. In sum, the president's Main Budget document should display and discuss the potential impacts of its policy proposals on its long-term projections in the same manner that it displays and discusses the potential impacts of the president's policy proposals on short- and medium-term projections, not hide these potential long-term impacts in a technical document.

3. **Revise the content and presentation of the president's budget documents.** I've mentioned above that bringing back the Citizen's Guide would help increase the relevance of the president's budget. And revising the content and presentation of the remaining budget documents could also help increase the budget's relevance. Three of the remaining seven documents—Federal Credit Supplement, Object Class Analysis, and Balances of Budget Authority (about 250 pages in total)—are strictly technical documents, available only online, that provide valuable data and don't need to be revised. Small revisions in each of the remaining four documents, however, could assist users and also improve the relevance of the president's budget:

- The Main Budget Document (about 200 pages). The president presents his budget proposals in this document and it should remain the primary place for the political arguments supporting the president's proposals. Adding long-term projections to this document and, perhaps, some of the political chapters currently in the Analytical Perspectives document (see below) are the only changes I would recommend.

- The Analytical Perspectives Document (about 400 pages). This used to be a technical document that included valuable information on several important topics, such as “Economic Assumptions and Interactions with the Budget”, “Federal Borrowing and Debt”, and “Tax Expenditures”. But lately political presentations that belong in the Main Budget document have been added. These include chapters on subjects such as “Strengthening the Federal Workforce” and “Federal Budget Exposure to Climate Risk”. Incorporating these political presentations into the Main Budget document—if the president deems this to be important—would cut the size of Analytical Perspectives by roughly a quarter and make both documents more focused.
- The Historical Tables (about 400 pages). During my long career at OMB, I often heard that this was the most useful budget document—a true reference source of valuable data available nowhere else. So why is it now available only online? The printed version should be restored immediately.
- The Appendix Document (about 1,400 pages). This document is prepared primarily for the Appropriation Committees. They need it and OMB staff needs to prepare it to make sure that the budget numbers are comprehensive and internally consistent, but there is no need to print it for anyone other than the Appropriation Committees.

With respect to implementing these changes, I recommend that a better way than putting them in legislation is to use the confirmation process for the OMB Director. Getting the agreement of the president’s nominee for OMB Director during the confirmation process can provide a personal commitment that Members can cite if the changes are not made as promised.

If I can close with one last point, it is time for a new budget concepts commission as former CBO Director Rudy Penner and I wrote last January.<sup>1</sup> The basic concepts underlying the U.S. government’s budget are in disarray. Consider that there is no generally accepted practice about how to deal with such things as what the budget should include, how spending and revenues are defined, or how the budget should be displayed to show the economic impact of different forms of spending.

The 1967 Report of the President’s Commission on Budget Concepts addressed some of these issues and led to some reforms, such as the unified budget. But many issues remain unresolved. It is time to create a new Commission to address several budget concepts, including:

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<sup>1</sup> “Time for a New Budget Concepts Commission” by Barry Anderson and Rudy Penner, Economic Studies at Brookings, No. 3, January 2016. See: <http://www.brookings.edu/research/papers/2016/01/11-budget-concepts-commission-anderson-penner>

- **The scope of the budget.** Some programs are “on budget” while others are “off budget.” Moreover, the way the budget should treat government sponsored enterprises and other government-private partnerships needs to be clarified.
- **Defining spending and revenue.** The distinction between taxes and spending has become muddled and needs to be addressed. For example, “tax expenditures” and “offsetting collections” should to be defined more precisely and their placement in the budget reconsidered.
- **The economic impact of different types of spending.** A new Commission needs to recommend better ways of showing the impact of such things as government purchases of securities, trust funds, capital investments, and loans or guarantees.

Although the topic of budget concepts may seem dry and technical to most Americans, and even lawmakers, almost all of these issues are important economically and have an important political dimension. How the budget is organized and its components defined and represented gives a particular impression about how much money the government raises and spends, and what it does with that money. So clarifying the way the budget is arranged and defining budget items has important implications. I urge the Committee to work with the President to form a new Budget Concept Commission.

I would be happy to answer any questions members of the Committee might have.



Chairman ENZI. Thank you. And the Ranking Member is here now, so I will call on Senator Whitehouse for his comments.

#### **OPENING STATEMENT OF SENATOR WHITEHOUSE**

Senator WHITEHOUSE. Thank you, Chairman. Let me again express my appreciation to you for the focus we have here on reforms that could improve our budget process and increase the relevance of this Committee. The hearings this month have been insightful, and I look forward to the rest of today's panel.

Setting aside the relative merits or demerits of a President's annual budget request, let me just take a moment on the document itself.

For as long as I have been a Senator, the President's budget has been a set of volumes, the first and the shortest of which is a summary that presents the President's policy vision. This is something of a political document, and I do not fault Republicans for viewing it at this time as dead on arrival. We did the same with the last two budgets sent up by President Bush.

While the first document can be viewed as a political or partisan publication, the other volumes include a wealth of information useful to all Members of Congress. These volumes include detailed, line-by-line tables of program spending at every agency, analyses of select policy issues, and historical tables listing budget information going back to the founding of the Republic.

At a recent hearing, the Chairman questioned whether anyone reads the entirety of the President's budget request. Probably not, but we should view most of the budget request as an annually updated encyclopedia of data on the Federal Government. Appropriators, authorizers, CRS, CBO, researchers, and academics all rely on this annually updated data and in many cases use language drafted by the administration and included in the budget request for appropriations and authorizing bills.

On the topic of the President's budget request, let me reiterate the dismay of Senate Democrats that the Chairman chose to break with tradition and not hold hearings on the President's fiscal year 2017 request. Congress may not always like the President's proposals, but for four decades, since the Budget Act's first passage, this Committee had never before denied the President the courtesy of hearing the administration out. Democrats heard out Republicans when we held the majority in the final 2 years of the Bush Presidency, and I hope the majority next year will restore this tradition, no matter who is President and no matter which party controls the Senate. It is an unprecedented and disorderly discourtesy.

Budget rules are only useful if we follow them, and this Committee is only relevant if we want it to be.

Last week, I had a useful and interesting conversation with the Chairman's friend, former Chairman Kent Conrad, where he described the respect that this Committee enjoyed during his early years in the Senate. According to Senator Conrad, it was not the rules that were different back then so much as simply that Senators actually took the budget and the budget process seriously, as we have not done for some time.

As we consider budget reform legislation, I would encourage the Chairman to bring in former Committee leaders, including Sen-

ators Conrad and Gregg, to get their takes on potential reforms. This could be in the form of a private meeting with members so that the conversation can be more open and less inhibited. I do think it would be useful to hear from the Senators who have sat in these seats in the past, and I do believe that we do need to make reforms in the way this Committee operates, whether it is to simply disable it and let the appropriators take over and the President and the leadership, or to turn it over to an ex officio committee of the Chairs of Finance and Appropriations and leadership and so forth, or whether to actually look at how this Committee works and revive it in more or less its current modality. But I do think that there are things that can be done, and I look forward to working with you. I think the bipartisan agreement in this area is very promising, and so thank you for that, Mr. Chairman.

Chairman ENZI. Well, thank you.

Senator WHITEHOUSE. I yield back to the witnesses.

Chairman ENZI. If I were trying to avoid criticism, I would never have had held this hearing. I think it is important and can bring out a lot of things that have been going on for actually decades. And if we cannot make it better, the country is in trouble. And we have to make it better together.

Mr. Capretta.

**STATEMENT OF JAMES C. CAPRETTA, SENIOR FELLOW, ETHICS AND PUBLIC POLICY CENTER, AMERICAN ENTERPRISE INSTITUTE**

Mr. CAPRETTA. Thank you, Mr. Chairman and Senator Whitehouse and the other members of the Committee. I am glad to be here. Thank you for inviting me to participate.

In my testimony today, I will discuss three aspects of the current process that require attention and reform: the uncontrolled growth of mandatory spending, the importance of keeping focus on long-term fiscal policy, and the absence of a process for facilitating legislative and executive agreement on the budget.

The fundamental problem with the Nation's finances is the runaway expense of mandatory spending programs. In 1962, the Federal Government spent 4.7 percent of GDP on benefit transfers and other automatic spending programs. By 2013, spending on these programs had risen to nearly 13 percent of GDP.

Instead of forcing policymakers to confront this problem, the current budget process shifts financial pressures off of these programs and onto other portions of the budget. As entitlement spending programs have gone up rapidly, funding for annually appropriated, discretionary accounts has fallen precipitously.

The next problem is the Nation's long-term fiscal policy. The Nation's fiscal position has deteriorated significantly in recent years, with large deficits and mounting debt. But the most significant threat is not short term but mid- to long term. According to the Congressional Budget Office, Federal debt will never again return to the post-war norm of below around 50 percent of GDP. Instead, the national debt will rise inexorably and exceed 100 percent of GDP in 2040. The primary cause, again, is rapidly growing entitlement spending.

Policymakers need to keep their eyes on the long run and the steps necessary to begin closing the immense gap between expected revenue and expected spending. It would be truly unfortunate if Congress and the President pursued a short-term fiscal plan without also thinking about what needs to be done over the longer term. The result could very well be a temporary reduction in the budget deficit that is quickly overwhelmed by long-term trends.

A related problem is that the executive and legislative branches of our Government have parallel budget processes that do not necessarily result in a consensus plan.

Congress expresses its views, when it does, on the budget in the congressional budget resolution. Congressional budget resolutions are not laws. Rather, they are concurrent resolutions, which means they are relevant only for the Congress. Presidents are in no way bound by them. Similarly, the President produces his own budget, and the Congress is not bound by it.

The parallel budgetary processes are a reflection of our constitutional structure. The co-equal branches each have a substantial role in the process, but there is no legal requirement that they ever come to an agreement. Indeed, with some exceptions, it can be said that the Federal Government never truly operates within a budget because the legislative and executive branches rarely agree on one.

A possible, partial antidote for budgetary drift, rising mandatory spending, and neglect of the long term might be found with a joint budget resolution.

Unlike a congressional budget resolution, a joint resolution must be agreed to by the President and, therefore, is a law. It thus has the potential, depending on its design, to facilitate, and perhaps even pressure, the legislative and executive branches into coming to an agreement.

There are numerous ways to provide for the consideration of a joint budget resolution, but the most straightforward option would be to build upon the current process. This can be accomplished by amending the current Budget Act rules to allow, at the Congress' discretion, an optional joint budget resolution to be spun off of a concurrent resolution, upon the agreement to it by both the House and Senate. It would then get sent to the President, and its contents, depending on what is in it, could be binding in certain ways on total discretionary spending, allocations for mandatory programs, revenues, deficits, and debt. The President could then either approve or veto a joint budget resolution.

A joint budget resolution covering the full budget would have the capacity to adjust the caps on discretionary spending, and I might note that this might be a place to start as an interim first step. A joint budget resolution could cover the whole panoply of things that are in the Federal budget, but it might be useful for the Congress to consider starting with adjustments just to the discretionary caps. At that point, when the Congress passed a congressional budget resolution, it would have the potential of automatically sending a law to the President, legislation to the President, adjusting the statutory caps, bringing into sync both the executive and legislative approaches to controlling discretionary spending. I offer that up as a potential first step.

I realize my time is about to run out here, so I am going to jump quickly to the long-term budget.

While a joint budget resolution with sensible enforcement would be a significant improvement over the current process, it will not by itself solve inattention to the long term. An important first step toward addressing that problem would be to get agreement between the legislative and executive branches on how to measure the long-term fiscal obligations of the Federal Government. That could be done by, first, starting with those known programs, the big ones—including Social Security and Medicare, but beyond that, the big Federal retirement and health benefit programs—measuring their unfunded liabilities over a period of time and getting agreement between the two branches of the Federal Government on exactly the methodology for making that calculation.

Once a common measure is established, it could be used to assess legislation in Congress and perhaps also be incorporated into a joint budget resolution. For instance, the budget process could be amended to require CBO assessments of how significant new budgetary legislation would alter the unfunded liabilities calculation.

Further, the congressional budget resolution might even allow the committees of jurisdiction to be reconciled for reductions in these unfunded liabilities, establishing a new way of using an expedited process to begin addressing the Government's long-term liabilities.

There are many other complications associated with reforming the process in these ways. I will stop now, and I would be happy to answer any questions. Thank you.

[The prepared statement of Mr. Capretta follows:]

Testimony Presented to the Senate Budget Committee  
United States Senate

“Proposals to Reform the President’s Budget and the Congressional Budget Process”

James C. Capretta  
Senior Fellow, Ethics and Public Policy Center,  
Visiting Fellow, American Enterprise Institute, and  
Affiliated Scholar, Mercatus Center at George Mason University

April 27, 2016

Mr. Chairman and members of the committee, thank you for inviting me to participate in this hearing.

The nation is facing serious fiscal challenges and has been for many years. The Congressional Budget Office’s (CBO) most recent long-term budget projections indicate that accumulated federal debt will reach 100 percent of the nation’s gross domestic product (GDP) in about two decades’ time. This is an unprecedented deterioration in the nation’s fiscal position. From 1957 to 2008, federal debt never exceeded 50 percent of GDP, but it now exceeds 70 percent of GDP. Over the next decade alone—2017 to 2026—the CBO estimates that the federal government will borrow another \$9.3 trillion, and that assumes spending on national security will fall to levels not seen since before World War II.

In my testimony today, I will discuss three aspects of the current process that require attention and reform:

1. The uncontrolled growth of mandatory spending;
2. The importance of keeping focus on long-term fiscal policy; and

3. The absence of a process for facilitating legislative and executive agreement on the budget.

### **The Role of Mandatory Spending**

The fundamental problem with the nation's finances is the runaway expense of mandatory spending programs. In 1962, the federal government spent 4.7 percent of GDP on benefit transfers and other automatic spending programs, such as Social Security, unemployment insurance, and welfare support. By 2013, spending on these mandatory programs had risen to nearly 13 percent of GDP.

Instead of forcing policymakers to confront the problem, the current budget process shifts financial pressures off of mandatory spending and onto other portions of the federal budget. As spending on entitlement programs soared since the early 1960s, funding for annually appropriated (or "discretionary") accounts, especially defense, fell precipitously, from 12.3 percent of GDP in 1962 to 7.2 percent in 2013.

Sooner or later, and probably sooner, the unsustainable nature of the current state of fiscal affairs will force change. A crisis might be precipitated by an international event that exposes the current defense budget as woefully inadequate to confront the threats to the nation's security. A quick upward adjustment in defense spending could set in motion changes in perceptions that lead to large increases in interest rates.

It would be far better for the country if elected leaders did not wait for a crisis to act but instead confronted the nation's fiscal problems with more foresight and planning. The changes in programs would be more gradual and more carefully designed.

**Keeping Focus on Long-Term Fiscal Policy**

The nation's fiscal position has deteriorated significantly in recent years, with large deficits and mounting debt. But the most significant threat is not short-term but mid- to long-term. According to the CBO's latest long-term projections, federal debt will never again return to the postwar norm. Instead, the national debt will rise inexorably and exceed 100 percent of GDP in 2040. The primary cause of unending federal deficits is rapidly rising entitlement spending. By 2040, the CBO expects spending on the major entitlement programs (Social Security, Medicare, and Medicaid), plus the subsidies made available by the Affordable Care Act, to total 14.2 percent of GDP, up from about 10 percent today. That is an immense shift of resources toward consumption-oriented entitlement spending.

Policymakers need to keep their eyes on the long run and the steps necessary to begin closing the immense gap between expected revenue and expected spending. It would be truly unfortunate if Congress and the president pursued a short-term fiscal plan without also thinking through what needs to be done over the longer term. The result could very easily be a temporary reduction in the budget deficit that is quickly overwhelmed by longer-term spending trends.

Unfortunately, the current budget process does not provide policymakers with a clear view of the long-term challenges, nor does it facilitate the kind of decision making that would improve the long-term fiscal outlook.

**An Elusive Federal Budget**

A related problem is that the executive and legislative branches of our government have parallel budget processes that do not necessarily result in a consensus plan.

Congress expresses its views on the budget in the congressional budget resolution (CBR). CBRs are not laws. Rather, they are concurrent resolutions, which means they are relevant only for Congress. Presidents are in no way bound by them and in fact have often denounced them as containing misplaced priorities. Of course, presidents prepare and submit a budget plan to Congress every year, and those too are often denounced as inadequate by members of the House and Senate.

The parallel budgetary processes of the executive and legislative branches are a reflection of our constitutional structure. The co-equal branches of government each have a substantial role over the federal budget, and there is no legal requirement that they ever fully come to an agreement with each other. Indeed, with some exceptions, it can be said that the federal government never truly operates within a budget because the legislative and executive branches rarely agree on one.

This structure has practical consequences. It is possible, and happens frequently, that Congress will proceed based on one budgetary framework, defined by a CBR, that differs substantially from the framework the president supports. The differences between the two branches get addressed, if they do at all, only when actual spending or tax legislation that is a product of the CBR framework makes its way all the way through the legislative process and reaches the president's desk. At that point, the president can sign or veto the legislation. Usually, if there is an ongoing disagreement, the anticipation of a veto is enough to bring the entire process to a standstill. This is an important reason why there are regular, drawn-out budget fights between Congress and the president. The two branches spend most of the year working from different budgetary plans, and then there is



a mad scramble to provide an ad hoc resolution to the disagreement to keep the government operating.

But even if an ad hoc process works temporarily, that is very different from having in place a budget framework that lasts multiple years and provides financial structure and stability to government finances. The current process does not apply any countervailing pressure to offset the institutional and political tendencies toward budget stalemate that are built directly into our constitutional order.

#### **The Joint Budget Resolution**

A possible, partial antidote for budgetary drift, rising mandatory spending, and neglect of long-term challenges might be found with a joint budget resolution (JBR).

Unlike a CBR, a joint resolution must be agreed to by the president and therefore is a law. It thus has the potential to facilitate, and perhaps even pressure, the legislative and executive branches into coming to an agreement on key budgetary aggregates that would govern decisions by both branches later in the budget process.

There are numerous ways to provide for the consideration of JBRs, but the most straightforward option would be to build on the current process. This can be accomplished by amending the current Budget Act rules to allow an optional JBR “spin-off” from any CBR agreed to by both the House and Senate. Congress would not have to pursue a JBR, but if it did so legislation would automatically get sent to the president upon adoption of a CBR, and the JBR would reflect the key budgetary aggregates: total discretionary spending, total mandatory spending, revenues, deficits, and debt. The president could then either approve or veto the legislation.

If the president vetoed the JBR, the process would revert back to what is in place today under the Budget Act. Congress could proceed under the terms of the budget resolution, and engagement with the executive branch would be postponed until later in the year, when the spending and tax bills flowing from that budget were transmitted to the president.

If, however, the president agreed to the JBR and signed it into law, the budget framework contained within it would have the force of law, and both branches would be bound by it.

A JBR covering the full budget would have the capacity to adjust the caps on discretionary spending, impose discipline on mandatory spending, and provide a target for revenues. This would ensure that Congress and the president truly engage in budgetary decision making. There would be clear trade-offs between the key budget categories, as well as projected deficit spending and debt. Congress and the president could choose to put more pressure on mandatory spending programs and thus perhaps ease the pressure on discretionary accounts, or vice versa.

Although ideally a JBR should cover all aspects of federal budget policy, it would be possible to start with an interim step of adjustments just to the discretionary caps. The CBR would operate as it does today, except that, upon adoption of a conference report on a CBR, Congress would have the option of sending to the president a JBR providing for adjustments to the discretionary caps at the levels provided for in the CBR.

This interim step would be important because it would empower the Budget Committees in the House and Senate; they would become the committees directly

responsible for establishing these binding caps—a first step toward a real budget process that would bind both the legislative and executive branches.

### **Enforcement**

The JBR concept works only if a sensible enforcement system is attached to it. The caps on discretionary spending are enforced with a well-established mechanism—a sequester of spending above the cap amount.

Enforcing discipline on mandatory spending is of course a more difficult matter. There are several ways to go about this, but whatever approach is chosen should:

- Provide an incentive for Congress to enact reform legislation that avoids the need for an enforced change in spending;
- Set in motion balanced and reasonable adjustments focused on many programs, not just an isolated few; and
- Allow for adjustments to occur over a period of years rather than all at once.

Congress could also choose other approaches to enforcement, such as focusing on the cancellation of future spending increases or planned program liberalizations scheduled to occur in future years.

### **Toward a Long-Term Budget**

While a JBR with sensible enforcement would be a significant improvement over the current process, it will not, by itself, solve the problem of inattention to the long term. An important first step toward addressing that problem would be to get agreement in the legislative and executive branches on how to measure the long-term fiscal obligations of

the government. That information could then be used to inform current legislative debates and eventually used to spur legislative action.

One approach would be to establish a uniform definition of the federal government's long-term unfunded liabilities. In general, this would mean calculating the present value of expected future tax receipts and expected future spending commitments. Long-term forecasts are already done annually for both the Social Security and Medicare programs, and so a large portion of the federal budget can be assessed on this basis with current information. (The latest projections indicate the combined unfunded liabilities for these programs is more than \$40 trillion.) These forecasts could be supplemented with assessments of other parts of the budget, especially those that create long-term obligations on behalf of the government, such as pension programs (civil and military and the Pension Benefit Guarantee Corporation) and health benefits.

Once a common measure is established, it could be used to assess legislation in Congress and perhaps also be incorporated into a JBR. For instance, the budget process could be amended to require CBO assessments of how significant new budgetary legislation would alter the unfunded liabilities calculation. Bills that would increase those liabilities could be ruled out of order and thus pulled from consideration unless a supermajority of the members chose to override the rule.

In addition, a CBR could "reconcile" the committees with jurisdiction over the major programs with large unfunded liabilities and thus set in motion privileged legislation to narrow the fiscal gap with corrective legislation. This kind of legislation would not need to show deficit reduction over a 10-year period but over some longer time frame, such as 25 or 50 years.

**Conclusion**

The United States is facing serious fiscal challenges that will not be easy to overcome. The sharing of budgetary responsibility by two co-equal branches of the federal government makes large-scale and painful change particularly difficult to achieve.

Moreover, budget process reforms cannot make political disagreements vanish.

But, if political leaders are inclined to search for an agreement on the budget, a better process could make it easier for them to reach that goal.

Chairman ENZI. Thank you.  
Mr. Collender.

**STATEMENT OF STAN COLLENDER, EXECUTIVE VICE  
PRESIDENT, QORVIS MSLGROUP**

Mr. COLLENDER. Thank you, Mr. Chairman, and let me apologize in advance for a cough that does not seem to want to leave. So if I cough, I am not dying.

Chairman ENZI. Okay. I think it is the pollen in the air.

Mr. COLLENDER. As a former intern and staff member of this Committee from back when it began more than 40 years ago, and as someone who has devoted much of his career to the Federal budget, I am, of course, delighted to provide the Committee with my views on improving the congressional budget process. But I cannot start my testimony with the standard line of commending the Committee for holding this hearing.

How is it possible that the Senate Budget Committee that earlier this year flatly refused to invite the Director of the Office of Management and Budget to testify, and in so doing helped render the Obama 2017 budget irrelevant, is now holding a hearing to discuss, in part, whether the President's budget is irrelevant and should be changed?

How is it possible that the same Senate Budget Committee that so far has refused to develop and vote on a budget resolution for the coming year is now holding a hearing to fix the budget process it refuses to follow?

To me, this hearing comes close to supplanting Leo Rosten's explanation of the word "chutzpah." Rosten said that chutzpah was when a man who is convicted of murdering his parents then begs for mercy from the court because he's an orphan.

Today this Committee is the fiscal policy equivalent of this man. After first preventing the budget process from being implemented this year, the Committee is now demanding the process be changed so it can implement it. That is chutzpah.

My response to the big question you are asking—How should the congressional budget process be changed?—is simple: Do not do it. The changes you make will have little positive impact on Congress' ability and willingness to develop and implement an annual budget. The budget process will be at least as inefficient and as infuriating with the changes you are considering as it is now.

In fact, Congress does not need a budget process at all. The U.S. Constitution gives the House and Senate all the power they need to develop, adopt, and implement a budget for the coming year. Congress can do whatever it wants right now. The problem is that the Senate Budget Committee, the full Senate, and Congress as a whole cannot figure out what they want to do.

So as this year's almost nonexistent budget debate amply shows, nothing happens. The country goes without a budget, without a fiscal policy that except by accident is relevant to the current and projected economy, without appropriations, and without many authorizations. Instead, we get shutdowns, threatened defaults, fiscal cliffs, and totally ignored deadlines. Instead of tinkering with the process, you should be trying to develop an overall consensus about what the budget process should do.

In fact, every previous congressional budget process was agreed to only when that type of consensus existed. In 1974, the Congressional Budget and Impoundment Control Act was adopted because there was an overwhelming agreement that Congress needed a process. The new process was outcome neutral; it could be used to increase or decrease the deficit and debt, and any combination of revenue and spending cuts and raises was acceptable.

Several years later, that outcome-neutral process was changed when there was a new consensus that reducing the deficit should be the goal. That deficit reduction process was itself revised when a consensus developed that Congress should only be held responsible for those parts of the budget within its immediate control. That is when we got PAYGO.

If you develop that missing consensus, it will be easy to design an effective budget process. Without it, any changes will be totally meaningless, uselessly symbolic, and a cynical hoax.

My prepared testimony includes comments on four specific budget process changes the Committee has recently mentioned: the need for authorizations, making the President sign a budget, doing away with the President's budget, and 2-year budgeting.

In the time I have left, I would like to discuss just this last idea, the plan to do a 2-year budget that supposedly will give Congress time to get everything done.

We have ample, direct precedent for knowing this will not work. In 1974, the Congressional Budget and Impoundment Control Act changed the start of the fiscal year from July 1 to October 1 to do exactly what you now say you want to do: give Congress enough time to get all of its work done and avoid continuing resolutions. But the only thing that this actually accomplished after the 1974 act went into place was to create a legislative rush in late September instead of late June. And continuing resolutions are even more prevalent now than they were back then.

My biggest fear, however, is not that the budget work in Congress will expand to fill the amount of time 2 years provides. It is that Congress at the same time will change the start of the fiscal year to January 1. If that January 1 start is after the election and there is a 2-year budget, Congress will never adopt a budget or be held accountable for passing one before voters go to the polls. That would be contrary to one of the major reasons the congressional budget process was established more than four decades ago. And it will be a political travesty.

I urge this Committee to stop any consideration of one-off process changes. Instead, focus on developing the consensus that today is completely absent from the budget debate. Until you do, hearings like this, sadly, will continue to be nothing more than diversions.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Collender follows:]

Testimony Of

**Stan Collender**

Before The  
Committee on the Budget  
United States Senate

April 27, 2016

Chairman Enzi, Senator Whitehouse and members of the committee:

As a former intern and staff member of this committee from back when it began more than 40 years ago, and as someone who has devoted much of his career to the federal budget, I am of course delighted to provide the committee with my views on improving the congressional budget process.

But I can't start my testimony with the standard line of commending the committee for holding this hearing.

How is it possible that the Senate Budget Committee that earlier this year flatly refused to invite the director of the Office of Management and Budget to testify and in so doing helped render the Obama 2017 budget irrelevant, is now holding a hearing to discuss, in part, whether the president's budget is irrelevant and should be changed?

How is it possible that the same Senate Budget Committee that so far has refused to develop and vote on a budget resolution for the coming year is now holding a hearing to fix the budget process it refuses to follow?

To me, this hearing comes close to supplanting Leo Rosten's explanation of the word "chutzpah" with a new instantly classic definition.

Rosten said that chutzpah was when a man who is convicted of murdering his parents then begs for mercy from the court because he's an orphan.

Today this committee is the fiscal policy equivalent of that man. After first preventing the budget process from being implemented, it is now demanding that the process be changed so the committee can implement it.

My response to the big question you're asking – how should the congressional budget process be changed at this moment – is simple: don't do it. Whatever you do is far more likely to hurt than help.



The changes you make will have little positive impact on Congress' ability and willingness to develop and implement an annual budget. The budget process will be at least as inefficient and infuriating with the changes you're considering as it is now.

The existing budget process is not the problem. In fact, Congress doesn't need a budget process at all. The U.S. Constitution gives the House and Senate all the power they need to develop, adopt and implement a budget for the coming year. Congress can do whatever it wants to do right now.

The problem is that the Senate Budget Committee, the full Senate and Congress as a whole can't figure out what they want to do and no one is willing to compromise.

So, as this year's almost nonexistent budget debate amply shows, nothing happens. The country goes without a budget, without a fiscal policy that except by accident is relevant to the current and projected economy, without appropriations and without many authorizations.

Instead we get shutdowns, threatened defaults, fiscal cliffs and totally ignored deadlines.

Instead of tinkering with the process, you should be developing a consensus about what the budget process should do.

Every previous congressional budget process was agreed to only when that type of consensus existed.

In 1974, the Congressional Budget and Impoundment Control Act was adopted because there was an overwhelming agreement that Congress needed a process. This new process was outcome neutral; it could be used to increase or decrease the deficit and debt and any combination of revenue and spending cuts and raises was acceptable.

Several years later that outcome-neutral process was changed when a new consensus developed in Congress that reducing the deficit should be the goal. That deficit reduction process was itself revised when a consensus developed that Congress should only be held responsible for those parts of the budget within its immediate control. As a result, the PAYGO rules were put in place.

All of the other subsequently adopted procedural changes occurred when a new consensus developed about what the congressional budget process should do and how it should do it.

There is no such consensus today. The 100 voting members of the Senate likely have 100 different ideas of what the budget process should accomplish. Add the

views of 435 members of the House and it's hardly surprising that the congressional budget process has become totally dysfunctional.

Develop that missing consensus and it will be easy to design a new budget process. Without it, any budget process changes will be totally meaningless, uselessly symbolic, and a cynical hoax.

I'd like to comment briefly on four of the budget process changes this committee has recently mentioned.

The first is the supposedly new requirement that all spending must be authorized.

The U.S. Constitution only requires that spending be appropriated. Authorizations were created by Congress to give members who weren't on the appropriations committees something to do. The fact that the authorization committees aren't doing what some expect and that the United States is surviving without authorizations is a strong indication that these bills may have outlived their usefulness.

Besides, Congress already has the all the power it needs to pass authorizations, so the fact that it's not doing that is a strong indication that it doesn't want to. And, as the other perpetually missed budget process deadlines show conclusively, procedural fixes will always be ignored when Congress doesn't want to do something.

The second is the now almost perennial proposal to change the congressional budget from a concurrent to a joint resolution so that it has to be signed by the president to go into effect.

This proposed change is totally misguided. It will so stymie the process that I can't help but think it's being suggested now solely for political reasons. The goal may well be to take the heat off Congress for not passing a budget by giving it the ability to send the president a ridiculous or hyperpartisan spending and revenue plan it knows she or he will veto.

The third is the plan to do away with the president's budget because it's too political.

Every president's budget is both a political and accounting statement and is far more than just tables and charts with columns of numbers.

But the same can be said for every congressional budget resolution and the report that accompanies it. And the budget hearings and debates in the House and Senate are almost completely political.

Budgeting is the most political thing Congress and the White House do...or is supposed to do...every year. As we've seen with every congressional or presidential budget commission, even with the best of intentions there's absolutely no way to remove the political considerations from any White House or congressional budget document or process.

The fourth is the two-year budget that supposedly will give Congress time to get everything done.

We have ample, direct precedent for knowing this won't work. In 1974, the Congressional Budget and Impoundment Control Act changed the start of the fiscal year from July 1 to October 1 to give Congress enough time to get all of its work done and avoid continuing resolutions. Four decades later we know the only thing this accomplished was to create a legislative rush in late September instead of late June. And, if anything, continuing resolutions are even more prevalent now than they were back then.

My biggest fear, however, isn't that the budget work in Congress will expand to fill the amount of time two years provides; it's that Congress at the same time will change the start of the fiscal year to January 1. If that January 1 start is after the election and there's a two-year budget, Congress will never have to adopt a budget or be held accountable for not passing one before voters go to the polls.

That would be contrary to one of the major reasons the congressional budget process was established more than four decades ago. It will also be a political travesty.

For all these reasons I urge this committee to stop any consideration of one-off process changes like these and instead focus on developing the consensus on the budget that is completely absent from the debate.

Until you do, hearings like this will continue to be nothing more than diversions for purely PR purposes.

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*The views expressed in this testimony are those of Stan Collender alone. They have not been reviewed or approved by any company or organization with which he is affiliated.*

Chairman ENZI. Thank you. I hope this does not just turn out to be a diversion. And since it has been raised several times, I did not do a hearing on the President's budget, but so far I have been able to prevent a vote on the President's budget, which the previous 6 years we have had. And, sadly, the President's budget total over the 6 years got one vote in favor. I thought that was an embarrassment. So like I say, I am trying to prevent the normal charade from continuing, and that's why we're all here today.

The idea with this is to wind up with something that helps to prioritize and move our country forward. I know that the President negotiated a grand budget—we passed a budget the previous year. But the President negotiated a grand deal in November, and that is different than the budget we agreed to. And so it does emphasize the point that the President needs to be involved at some point earlier.

Of course, this budget that he did present, which was 3 months after the grand deal, exceeds the grand deal that he made in November. So that presents a few difficulties of its own, and the discussion of those would probably not be really helpful because we are in another process here of trying to figure out how we can set some priorities for our country.

Mr. Capretta, the congressional budget resolution is not signed by the President, as you pointed out, and he is not directly involved in the budget negotiations, at least not until the need for a grand deal. As you pointed out, this leads to disagreement between the legislative and the executive branch on the priorities and creates crisis negotiations.

Can you explain a little more how the congressional budget resolution and that spinoff joint budget resolution might provide some kind of a long-term framework?

Mr. CAPRETTA. Well, one could imagine that the—for instance, around the total level of discretionary spending, let us assume that the congressional budget resolution did allow for a spinoff bill to go to the President on the level of total spending in those bills—in the resolution that would go to the President and adjust the caps, perhaps for a multi-year period. If that were the case, suddenly the congressional budget resolution would take on a lot more importance from the executive branch's perspective because the caps—the bill that would be sent down to the President for signature or veto would be real and binding on the executive branch. It would not be just something to not take seriously and ignore and maybe in many ways, you know, criticize and denounce is not adequate, et cetera. And so that would make the congressional budget resolution, at least on that aspect of it, very real and very pertinent, and I think would probably in certain circumstances lead to a discussion, negotiation, and give-and-take earlier in the year.

Now, I would like to say that Mr. Collender's points about, you know, process not preceding policy I think is basically right. I have in my written testimony—I was not able to say it in my oral presentation—I do not think process can be a substitute for political disagreement. If there is just no agreement between the two parties and the two branches, no process is going to make them agree. The only thing that makes them agree is the fact that you have to fund the Government at some point, the possibility of a shutdown.

And so that is the precipitating event in recent years, and that would still be the case even under this.

There is no reason—you know, the President could always veto a joint budget resolution. So there is nothing necessarily in this that would make agreement a requirement.

On the other hand, if you just look at today's process, there is nothing that is set in motion to even allow an early agreement. And so this at least would have the possibility, if the two sides were so inclined, to come to an agreement earlier rather than later.

Chairman ENZI. Thank you.

Mr. Anderson, you pointed out that the national debt is projected to exceed GDP by 2040 and the President and Congress face a unique challenge in addressing this issue because 2040 is outside of any 10-year budget window that we use to measure the spending and revenues. And so you have argued also for a long-term budget projection.

How would an emphasis on the long-term budget proposal impact the budgetary decisionmaking? And what are some key elements that should be included in that proposal?

Mr. ANDERSON. Mr. Chairman, in your introductory statements, you had a slide that indicated how much of current spending is now mandatory. I believe it was 70 percent is mandatory, 30 percent is annual discretionary. I go back many years, Mr. Chairman, and back when I first started out in budgeting, it was almost exactly the opposite; that is, we had close to 70 percent in annually appropriated funds and only 30 percent in mandatory spending. But the situation you painted accurately now does not portray what is going to happen in the future; that is, that portion of the mandatory spending is going to grow even further, shrinking the importance of the discretionary spending.

With this in mind, I think there are five fundamental principles one should look to towards long-term budgeting:

First, that long-term fiscal sustainability is necessary to promote long-term economic growth and better standards of living for the country. If you want a good example of that internationally, it is Japan. They do not have long-term fiscal sustainability, and they have had now two, going on three decades of low, if not declining economic growth.

The second principle is that, in order to obtain long term fiscal sustainability, long-term projections are necessary. Certainly they should be transparent and have sensitivity analysis, but it is absolutely necessary to have them.

The third is that, in order to obtain long-term fiscal sustainability, you do need some kind of constraints. I happen to believe that the PAYGO mechanism is inferior to caps on spending and that my experience with Sweden and a few other countries indicates that caps on spending can work. And, in fact, right now we have some kind of caps on tax expenditures. One is called the alternative minimum tax and the other is the Pease limitation on Schedule A itemized deductions. But we do not have any caps on the other major drivers of our long-term fiscal insustainability, the health programs and Social Security.

Fourth is that simplicity matters. The complexity that we have just is so hard to explain when it is all wrapped in spin, and, therefore, a simple presentation matters.

And, lastly, the effort of the Congress and the President and the public ought to be to concentrate on what works. We have too little attention on the effectiveness of programs and too much attention on how much spending is going into them or the input as opposed to the output or outcome.

So that is how I would change the long-term presentation.

Chairman ENZI. Thank you. My time has expired.

Senator Whitehouse.

Senator WHITEHOUSE. Thank you, Chairman.

I take somewhat to heart Mr. Collender's warning that the problem is that the Senate Budget Committee, the full Senate, and Congress as a whole cannot figure out what they want to do and no one is willing to compromise. He draws the conclusion from that changing the procedures here will not have an effect, and that is where I must say I differ. I do think that there are ways in which by empowering process, ideas and individual leadership can be brought to the fore in healthier ways than the present process permits.

The United States Constitution is a process document. Then came the Bill of Rights, which moved a whole lot of more substantive rights into the equation. But the original Constitution was a process document. I believe process matters, and I think we can do a lot better.

There are a couple of areas that I would like to ask the witnesses to consider, and please do not—we are not going to have time for you to consider these right here in the hearing, but we are trying to build a record of ideas, so please do get back to us. I will make these questions for the record.

I think the simplest thing we can do is solve the problem of vote-a-rama. When the budget process for every Senator is associated with tiresome mischief and nonsense, it is hard to undo that association and say, "Okay, now we are serious." So removing the tiresome mischief and nonsense from the very undignified vote-a-rama process I think is something that we actually can agree on. Is that a big achievement? No. But I think it is an important start.

The second thing I think that we should think about—and, again, this is all in terms of—we would like to have your responses. I think it helps if we actually push down a little bit further in the budget so that any budget that we have to come up with here gets applied to accounts within the appropriations level. Obviously, it is not going to be binding on appropriators. They can do whatever they please. But if a budget is pure hypothetical theater, at the most macro level, and nobody is responsible for applying it to every account, then what you end up with is people meeting with advocacy groups saying, "I am for you. Do not worry. We will protect you."

Well, no, because they say that to every single group that comes in, but none of that is true in the context of the overall proposal that has been made. So you have got to—it is a measure of accountability to have the budget actually connect to appropriations

accounts so people have to own what they are proposing one way or the other.

A third is that, for me, the ideal goal would be that we could agree on three things. Thing 1 would be that we could find a way to agree on what an appropriate debt-to-GDP ratio is. And if we can agree on what an appropriate debt-to-GDP ratio is, we would then need to agree on a glide slope to get to it without too much of a brute shock to the economic system. And if we can agree on a debt-to-GDP ratio and a glide slope to get from where we are to that, then we would need to build fences so that there would be consequences of failure. If we can do those three things, I think that markets and Congress would take some assurance that, okay, we have got some degree of method for solving this problem rather than having it just be a free-for-all in which a lot of political posturing takes the place of policy development.

The last point is that if we are going to do this, we cannot do it just looking at the expenditure discretionary piece of our budget picture. We have to look at tax expenditures. They are enormous. And we have to look at the cost of our social programs. And the thing that comes most readily to mind is the importance of health care costs, which witness after witness after witness after witness has said is what is really driving all of this. So we can get by okay, but health care cost is going to just go crazy. The projections are alarming, and where do we go? I think we are up 100 times on national health care costs just in my lifetime. It is a big number.

So how do we do that? I think if you are planning ahead, there are ways to look at health care savings and think systemically of how you make a health care system that is not the world's outlier for cost per capita by a huge margin compared to very well developed OECD countries that have robust and healthful health care systems. If we wait until the last minute and then the only tool we are left with is cutting benefits for seniors on Medicare, well, that is not going to go anywhere. We have got to have a way of looking at this as a systemic problem.

So I think if we can work our way through some of those things, I am actually pretty optimistic that we can get this done. I think a lot of people in the Senate want it to get done, and I think that we have an opportunity through reforms to make that environment more hospitable so that people who want to lead in this area and can bring their colleagues away from brinkmanship have a means for doing so, because right now the means is the President, the Republican leadership in the House and Senate, the Democratic leadership in the House and Senate all go in a room someplace, and they wheel and they deal, and God knows what side deals are cut to make people happy, and the rest of us get presented something, there it is, you have 3 days to look at it, or 3 hours to look at it, and then we are all going to vote on it. I think there is a huge majority of Members in the House and Senate who think that that is a really crummy way to do business and that their voices and their constituents' voices are completely eliminated in that process.

So I see a pretty significant motivation to get this done, and I am more positive than Mr. Collender, I would say. Your concerns and cautions are notable, and your experience here is laudable. I just wanted to let you know I am a little bit more optimistic.

Chairman ENZI. And I appreciate your optimism, but I think it is backed by the ideas that you presented there. Of course, the devil is always in the details.

Senator WHITEHOUSE. Yes.

Chairman ENZI. And we need to get to some of those details and see how to do them. I am optimistic for our country, and I feel serious enough about this that I volunteered to eliminate the Budget Committee if it is irrelevant.

Senator WHITEHOUSE. Yes.

Chairman ENZI. We do not need more steps in our process. We need more effective steps in our process.

Senator WHITEHOUSE. That should be one of the options that we consider.

Chairman ENZI. Continuing on with questions, Mr. Capretta, the congressional budget resolution has not been effective in controlling any mandatory spending. I think one of the reasons we had it as part of the comprehensive budget before was because it was generating revenue for the rest of the things because we had more money coming into Social Security than was going out. But that is not the case anymore. The budget is enforced through procedural points of order that only require 60 votes to waive. As I mentioned before, it is the same as required to end debate, and offsets to new spending often do not result in real savings. So automatic mandatory spending has grown to this 70 percent.

What enforcement mechanisms should Congress implement to enforce the mandatory spending levels in the budget resolution?

Mr. CAPRETTA. Well, it would have to be done in conjunction with the President, so an enforcement mechanism that was inside just the Congress could only be a rules based approach. Prohibiting the consideration of any legislation that might increase spending on any entitlement programs until such time as the spending was brought in line with the budget plan, that would be one thing you could do. But that is not nearly as effective as something that would have the agreement of the executive branch and would bring about real consequences unless some new legislation was passed to reform the program and bring it into conformity with a budget plan.

In terms of enforcing that, that is the million-dollar question because it is highly, highly controversial. How do you keep spending on programs that are automatically occurring in line with a budget that is below a projected baseline? Obviously, that will entail a lot of political controversy.

I think the easiest things to do are to cancel future increases in spending until such time as new legislation comes in to bring a program in line with its budget. You could apply an across-the-board spending cut. When those have been designed in the past, large chunks of mandatory programs get exempted from it through the political process establishing the sequester. And then you end up with a very narrow base and a very large cut, and that ends up being not very effective.

So I grant that this is the most difficult part of a more enforceable budget plan. It requires a lot of bipartisan patience to work through it all. I think the goal should be as I outlined in my testimony: cancellation of future spending increases first, broad-based,



as much as possible, spending reductions so you do not exempt a lot of programs. You are going to have to exempt some for very vulnerable populations, but targeting the budget also in a way that is realistic and consistent with a prudent approach to reining in future spending growth.

Chairman ENZI. Thank you.

One of the suggestions that I have been working on is that maybe mandatory programs ought to be limited to those that have a source of revenue that covers their costs annually, and everything else would come under the jurisdiction of budget and appropriations.

While I have Mr. Anderson here and he has experience with other countries, I did want to see what he has seen from experiences with the budget processes in other countries that would contain features that might help us in our process.

Mr. ANDERSON. Thank you, Mr. Chairman. I want to answer in three different ways.

First of all, with respect to Senator Whitehouse and his ideal goals, we have a very good example of how those ideal goals do not work in Europe. The European Monetary Union—that is, the countries that use the euro—includes almost all the Western European countries except the U.K., Denmark, Sweden, Norway, and Switzerland. They set up a process similar to what Senator Whitehouse just described; that is, they started with a politically established debt-to-GDP ratio. Then they set up a glide path how to reach it. But what they did not do—and what Mr. Capretta just mentioned—was build effective enforcement mechanisms, and a result you can see not just from their debt or deficits but also from their economic performance.

I would like to mention two other countries, one is Sweden. Sweden suffered in 1995 a financial downturn even worse than what we have suffered in the past 10 years. And what they did was vastly reorganize their budgetary status and processes. Again, they are part of the European Union, but not members of the European Monetary Union. They do not have the euro there.

One of the things they did was set up 27 different categories of spending. That included every element of spending, including mandatory spending. Then they set up enforcement mechanisms. The enforcement mechanisms were the equivalent of “lookback sequesters.” They do not call them that, but they looked back in the next year at whether the targets were met or not.

What they did not do in the beginning, however, was include tax expenditures. They realized what a mistake that was.

Senator WHITEHOUSE. What a mistake it was not to include them.

Mr. ANDERSON. Tax expenditures are a relatively new concept in budgeting. We in the U.S. are the ones who created it, I think, about 30 years ago. Sweden had them and did not realize that they needed to control them. Once they set limits on these 27 different categories of spending then they realized that they had to control tax expenditures.

In one sense we are lucky here. We already have a modest type of caps on tax expenditures. They could be improved considerably. That is, through the alternative minimum tax and the hair cut that

one needs to take on the Schedule A deductions, there is some modification of the amount of tax expenditures. It might need to be improved. But what we do not have is any kind of limit at all on the other three major drivers of our long-term unsustainable fiscal outlook: Medicaid, Medicare, and Social Security. In response to your question, Mr. Chairman, Sweden does, and they have had a very good result from it.

Lastly, I would like to mention Australia. Australia 15 years ago established long-term budget projections that go out for 40 years. And they use them in their budget process. Every couple of years, they look at what their original projections were and how the new projections are different and what are the reasons for those changes. They then try to understand the reasons for those changes in order to modify future legislation.

So in the Committee's consideration of budget process changes, keep in mind the European Monetary Union, Sweden, and Australia is what I would recommend.

Chairman ENZI. Thank you. My time, again, has grossly expired. Senator Whitehouse.

Senator WHITEHOUSE. I guess the last point that I would emphasize for your written comments, or if you have anything you urgently want to say, please feel free to do that now, is this problem of health care cost. There are two graphs that I think of all the time when I think about health care cost. One is the one I referred to earlier of all of the OECD nations, and the Y axis is life expectancy, and the X axis is per capita cost of health care. And the United States is a crazy, wild outlier on per capita cost in health care, miles from the most inefficient other OECD country in the world. And you would think, "Okay, cool, that is great. That means that we are spending all this money, but, wow, are we healthier. We must be living super long lives. America is great." And then you dial back and look where we are on the Y axis, and we are like Croatia or Greece. We are not leaders of the pack by any stretch. We are barely holding our own in the middle of the pack. So that is, to me, a signal that there is an opportunity for cost savings in health care that do not require benefit cuts, which is sort of Civil War medicine applied to a much more complicated problem.

The second is the distribution of cost per capita for Medicare State by State, and that is all over the place. And you can draw more or less a midline through that, and you could even draw a little bit of a safety belt bandwidth around the midpoint, and then I think you could start to look at the outliers and say, "Why is it that we are paying this State this much money for Medicare and Medicaid when they are costing significantly more per capita than other States?" We know you can do better because other States are doing better. It tends to be the Northern States that do better—I do not know why—and Hawaii, and it tends to be the Southern States that are vastly more expensive than the Northern States. But if you make that a State problem, it seems to me, by saying, okay, everybody gets a hair cut to the extent that you are outside of our bandwidth, every practitioner, every hospital, every doctor, everybody—we are not going to do it right now. We are going to give you 3 or 4 years to prepare yourself for this. But you can bet that the medical society in that State, the hospital association in

that State, the Governor of that State, the health director of that State are all going to start looking around in a new way and saying, Damn, why are we so bad? Why are we the McAllen, Texas, to use Atul Gawande's example, compared to El Paso or someplace else in Texas that is way cheaper? And the doctors in the cheaper places are going to look down at the McAllen doctors and say, Hey, you clowns, knock it off, you are costing us money now; this is not just fun and games.

And so I think that there are real opportunities to put pressure on these outliers and bring our outlier OECD status back in. And one of the happy things about pursuing that strategy is that over and over and over it has been shown that when you bring down the cost of care by improving quality, you actually have happier patients and better care and better outcomes and all of that. It is an unusual win-win-type virtuous circle if you can get yourself into it. But there has to be really an incentive to get people into it because the power of the status quo is very strong.

So I emphasize that I do think there are things that can be done within the context of the big social programs that we have to reduce their cost that do not end up with us pointing fingers at each other over who is trying to cut benefits for the elderly. There are plenty of ways we can do it better. We are just beginning to learn it. The way we pay for health care is going to have a lot to do with how we make that happen. But I do not think that it is conceptually beyond the scope of the Budget Committee to say, based on solid testimony and good bipartisan support, you know, we think this really can be done. And we are going to put some caps out there, and we are going to demand that the authorizing committees and the appropriating committees drive towards it. And, by the way, if you cannot come up with something yourself, here is the way we can offer you that we think will help work. If you can do better, you are the authorizers. If you can do better, you are the appropriators. Great. Go for it. But if you cannot, if you are going to continue to muddle along like this, we have got a backstop, and here is our backstop.

So I think there are some ways to address even those very difficult and challenging areas without getting into the usual partisan knife fights over them.

So thank you again, Chairman, for the hearing. I do think that the witnesses have been very helpful to us. I look forward to their commentary back. As I said, at least on our side, and I think on the Chairman's side as well, he has notes that he takes, and then he goes back, and when he thinks something is particularly good, he draws circles around them. He has described that process before, and hands them off, and I think we are doing a deliberate job of trying to put a book together of ideas and strategies so that we can have a really productive conversation as a Committee and decide where to go. And I think do not feel that you are sending these things to be put on a dusty shelf someplace with most of the other Federal written product, never read again. I think we will—you have our attention, and we appreciate it.

Chairman ENZI. And we have a tentative comment by the Majority Leader that at the conclusion of the 12 appropriations, he will allow us to consider whatever we come up with.

Senator WHITEHOUSE. That would be very good.

Chairman ENZI. So we have got some incentive to get it done—and, again, before the elections when nobody knows what the outcomes are going to be. And I feel real bad, Mr. Collender. You have not had another opportunity to speak. I would love to give you an opportunity to talk about anything in the budget process that you would like to. I do appreciate your testimony even though it felt a little directed. [Laughter.]

Mr. COLLENDER. Please do not take it personally, Mr. Chairman. It was written with a great deal of respect and appreciation for your efforts. But I just felt a need to get it out of my system.

Chairman ENZI. Sure.

Mr. COLLENDER. The one thing that I would urge you both is to understand that our 40 years of experience with the congressional budget process shows conclusively—and not just the budget process but every budget commission that we have put together—that you cannot take the politics out of the budgeting process. In fact, the budget is the most political of all the things that Congress does. If there was enough money to do everything that everybody wanted to do, you would not need a budget process. You would just need a check writer. Once you decide that there is not enough money or you are not willing to provide enough money for everything that everybody wants to do, the question is: How do you decide? And in this environment, particularly these days, with relatively narrow majorities and hyper-partisanship, all of the procedural changes you have discussed will never be implemented. That is, you will put together a budget process that may pass and will then be ignored within seconds.

As a quick example, in 1974, the budget process came together. It was done for a point in time. It was eventually implemented starting in 1976. The first year it was implemented, Congress balked at doing it. Members who voted for the budget process—and it passed unanimously in the Senate and with six dissenting votes in the House—a year earlier all of a sudden realized, “Oh, my God, I have got to vote for the deficit for the first time,” and they said, “No, I am not going to do it.” Had it not been for the intervention of the leadership—at the time in the House, it was Dick Bolling, Chairman of the Rules Committee and Tip O’Neill as Speaker—the budget process would have died the year after it was created.

The same thing is true with virtually every other budget process; it is good when it is passed because it solves a political problem at that particular moment. But then it starts being changed or people start having plans for it to change within seconds. Gramm-Rudman-Hollings was revised 2 years after it was put in place. And then the revised Gramm-Rudman-Hollings was revised 3 years after that.

Forgive me, but it is a little naive to think that you can put together a budget process that will last for all time. You would be lucky to get it through for just one session of Congress. And forgive me for being disrespectful.

Chairman ENZI. Well, you are not, and I appreciate your comments. I have to tell you, though, that in order to serve in the United States Senate, you have to be an ultimate optimist. [Laughter.]

Because, otherwise, after you bang your head against the wall for years on one topic, you might finally get it done. And if you give up earlier than that, it does not get done. So you have been working on this health care for a long time, and hopefully we will listen now.

Senator WHITEHOUSE. Yeah.

Chairman ENZI. I think it would have made a huge difference in what we have, had you had some of those things.

Senator WHITEHOUSE. Yeah.

Chairman ENZI. And to your comments on they always fail, I have done a lot of research on the previous processes and the changes that we have made, and I started doing it because I noticed that the format that we have the budget in and the format that Appropriations uses and the format that the President presents his budget in are all different. And through my research, I found out that it was intentional. It is so that you cannot follow the dollars, so that there is more flexibility, more capability to avoid any kind of constraints. And I think that Senator Whitehouse has come up with a good list, and we have got a good list from other members of the Committee. We will have to see if we can plug in details that will work. And as the ultimate optimist, maybe we can get one that they will actually listen to.

So I appreciate the testimony of all three of you. Your whole statements will be a part of the record and be shared, and people have until 5 o'clock today to turn any other questions in that they want to have answered. So thank you very much. The hearing is adjourned.

Senator WHITEHOUSE. Thank you, Chairman.

[Whereupon, at 11:44 a.m., the Committee was adjourned.]

Questions for the Record

For

**Barry Anderson**

*“Better Budgets, Better Results”*

April 27, 2016

*Senate Budget Committee*

**Questions from Chairman Enzi**

Question #1:

One of the primary purposes of a budget document, such as the President’s Budget Proposal or the Budget Resolution, is to provide information on the financial state of the nation. There are several budgetary concepts that are not adequately defined or reflected in the current budget documents.

What would you recommend a new budget concepts commission consider? And, how would this information better inform the budget decision making process?

Response:

I believe that a complete list of issues that might be considered by a new Commission should be decided by the Commission itself, but below is a sample of important issues that should draw the Commission’s interest.<sup>1</sup> And of these issues, **the ones dealing with Fannie Mae and Freddie Mac, federal regulations, tax expenditures, and the accounting for loans and guarantees could dramatically change budget scoring thereby better informing the budget decision-making process.**

The main issues that the Commission should consider fit within three broad categories: the proper scope of the budget, the definition of spending and revenues, and techniques for displaying budget items so that the economic impacts of these issues can be better understood.

**Scope of the Budget**

As the 1967 Commission recommended, the budget should encompass the full scope of federal programs and public-private entities. The Commission suggested certain broad criteria to help make such determinations. For example, who owns an entity and selects the managers? Does

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<sup>1</sup> The response to this question is largely taken from “Time for a New Budget Concepts Commission”, by Barry Anderson and Rudy Penner, Economic Studies at Brookings: A Series of Discussion Papers on Re-Imagining the Federal Budget Process, No. 3, January 2016.

the Congress and the President have control over an entity's program and budget, or are its policies set primarily in response to the goals of its private owners while ignoring the pursuit of broader public purposes?

Despite the broad scope of the 1967 Commission's guidelines, they do not clarify the appropriate budgetary treatment of certain partnerships between the federal government and the private sector. A new Commission needs to address this. Still, it is particularly difficult to deal with government sponsored enterprises (GSEs), such as Fannie Mae and Freddie Mac. They are owned privately but have dual public and private roles. Some of their directors are appointed by the government. Although government guarantees cover only a tiny portion of their potential liabilities, it is generally believed by those who follow the activities of GSEs that they will be bailed out by taxpayers if they run into financial trouble—exactly what happened during the Great Recession. A new Commission should be able to devise measures of the risks that such institutions impose on the taxpayer thus making an implicit guarantee more transparent.

Some new entities that mix private and public purposes may be created soon. For example, there are many proposals for an infrastructure bank with different plans having different degrees of private involvement. To the extent that such entities proliferate, it becomes more important to decide how they should be handled in budget documents.

Somewhat different issues arise with enterprises that are wholly owned by the U.S. government but are not now on-budget. For example, the business operations of Amtrak are generally excluded from the federal budget, but Amtrak's board members are appointed by the President, its preferred stock is owned by the Department of Transportation, and the federal government controls the routes that Amtrak uses. In addition, Amtrak has not earned any profits in its more than 40 years of existence. The Nation's economic system would not permit any truly private entity to last under those conditions. Other examples of hybrid public/private entities include the Metropolitan Washington Airports Authority and agricultural marketing boards. Currently subsidies to such entities are on-budget, but the Commission might consider including their gross revenues and spending in budget totals.

If lawmakers determine that the federal budget should continue to exclude such entities, then perhaps a new or more complete list of criteria should be developed to better distinguish between federal and non-federal entities for budgetary purposes.

There was a time when some agencies, such as the Export-Import Bank, were "off-budget," but this has become less frequent in recent years. However, the Social Security system and the U.S. Post Office are now officially off-budget. Nevertheless, the deficit concept that gets most attention is the unified budget deficit, and this includes the operations of Social Security trust funds. Being off-budget is mainly important for procedural reasons. For instance, Social Security cannot be subjected to reconciliation, a procedure that can be used to reform other entitlements. As a general rule, the Commission should not get into such matters of budget

process, but Social Security is the government's single largest program, and giving it a special status that makes reform more difficult seems hard to justify.

Should the budget identify some costs of regulation? Regulation is often a close substitute for a government spending program when used to mandate that private or state and local sectors spend to achieve social or economic goals. A committee to examine the budget process, created by the Bipartisan Policy Center and headed by former Senator Pete Domenici and former OMB and CBO Director Alice Rivlin, has suggested that analyses of regulatory costs should be part of the budget process.<sup>2</sup> Reflecting such costs in the budget itself would be difficult conceptually, but that doesn't make them any less real. The Commission might consider addressing regulation by adding a budget document that reports on cost and benefit studies of some of the most important regulations issued each year. This would at least provide useful information to the public and lawmakers considering the budget.

#### **Definition of Spending and Revenues**

Over the past 30 or more years the distinction between taxes and spending has become muddled. Maintaining a consistent and clear distinction in the budget between spending and taxes would give lawmakers and the public a more accurate picture of the size of the federal government and the amount of budgetary resources it obligates.

*Tax Expenditures.* For example, the tax code is riddled with credits against tax liabilities, as well as deductions and exclusions from taxable income that are intended to encourage taxpayers to pursue a diverse array of public policy goals. Often, the goals could be pursued equally well by spending programs, and tax expenditures are the equivalent of such spending. But these tax credits, exclusions, and deductions generally show up in the budget as a revenue reduction and so can give a misleading impression of government activity to the public and lawmakers. There is an exception to this rule: if a tax credit exceeds a taxpayer's other tax liabilities and is deemed to be "refundable", a money payment is made to the taxpayer. That payment appears on the spending side of the budget. If the entire value of credits, deductions, and exclusions was considered to be spending, government would appear to be much larger relative to the size of the economy, and there would be a clearer sense of government priorities.

Tax credits now exist for such diverse activities as the production of alternative fuels, reforestation, education, and income support. There are deductions for mortgage interest, state and local tax payments, and charities among other things. Municipal bond interest is excluded from income, and the list of special tax provisions goes on and on.

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<sup>2</sup> Rivlin, Alice M., and Pete Domenici. *Proposal for Improving the Congressional Budget Process*. Bipartisan Policy Center, July, 2015.



But there is a certain arbitrary element in the definition of a “tax expenditure”. Most commonly it is defined as any departure from a pure income tax with a specified rate structure.<sup>3</sup> Alternatively, it could be defined as a departure from a pure consumption tax with a specified rate structure. A new Commission might decide to use more than one definition of tax expenditures and, regardless of the definition, it would have to decide on the best way to display them.

*Offsetting Collections.* The distinction between revenues and offsetting collections, which are treated as offsets to spending, is also a concern. Offsetting collections from the public typically are linked to a business-type activity or service provided to the public by a federal agency. In the budget process, they are distinguished from revenues collected under the federal government’s sovereign power to tax or regulate. Over the years, laws have been enacted that classify certain revenues as offsetting collections. However, revenues that are improperly classified as an offset to spending provide a distorted picture of government finances.

A prominent example are the fees collected by the Securities and Exchange Commission (SEC). These fees should be classified as revenues, not as offsetting collections, because they are collected (as are other taxes) under the government’s sovereign powers, not because they are associated with a business-type transaction. However, laws have been enacted requiring some of the fees to be counted as offsetting collections and credited to the appropriation account for SEC salaries and expenses, although some existing SEC fees are recorded as governmental receipts (that is, revenues). Another example involves the premiums collected for Medicare Part B. They are classified as offsetting receipts, and Medicare outlays are often reported net of those fees. This significantly understates the scale and economic importance of the program.<sup>4</sup>

#### **Budget Displays That Clarify the Economic Impact of Different Types of Spending**

The 1967 Commission called for developing budget concepts that provide “the public with information about the national economy essential for private business, labor, agriculture, and other groups.”<sup>5</sup> This is as much an issue today as it was 50 years ago. The same dollar outlays spent on different programs can have very different effects on aggregate demand in the economy in the short run and on economic efficiency in the long run. It is impractical to account for all of these differences in budget displays, but there are cases in which the differences are so extreme that it may be useful to account for them differently.

<sup>3</sup> OECD, “Tax Expenditures in OECD Countries”, OECD Publishing. January 5, 2010. “The Distribution of Major Tax Expenditures in the Individual Income Tax System”, Congressional Budget Office, May 29, 2013.

<sup>4</sup> For a detailed discussion, see “Federal User Fees: Key Considerations for Designing and Implementing Regulatory Fees.” GAO. 2015. & “Federal User Fees: A Design Guide.” GAO. 2003.

<sup>5</sup> “Report of the President’s Commission on Budget Concepts”. US Government Printing Office, 1967.

*Purchases of Securities.* Take government purchases of private securities, including corporate bonds and equities, as an example. Such purchases are a part of some proposals to reform Social Security. Under current budgetary guidelines, purchases of private financial securities are recorded as cash outlays; the sales of the securities and returns on them (such as dividends and interest payments) are recorded as offsetting receipts. The budgetary treatment is the same for investments in private financial securities as it is for investments in non-financial assets.<sup>6</sup>

On the one hand, important distinctions exist between financial and non-financial assets. In general, financial assets are acquired to generate a flow of income rather than to provide public services, such as national security, health care, or recreation. That distinction suggests that government purchases of private equities should be treated differently in the budget than purchases of nonfinancial assets. On the other hand, if equity purchases were not counted as outlays, the budget would not accurately reflect the level of the federal government's ownership and control of private sector assets. That omission would seem to violate one of the fundamental principles of the 1967 Commission—that the budget should reflect the true extent of the government's interactions with the economy. The differences in the Office of Management and Budget (OMB) and Congressional Budget Office (CBO) treatments of the federal government's receivership of Fannie Mae and its impact on the economy is another example of the importance of having an accepted principle for the government's acquisition of financial assets.

*Trust Funds.* The federal government accounts for its activities through two broad groups of funds: federal funds and trust funds. In general, trust funds are created in law to earmark receipts for specific programs and purposes. The General Accounting Office in 2001 identified more than 200 trust funds in the federal budget, although fewer than a dozen account for the vast majority of trust fund receipts and spending.<sup>7</sup>

There are other ways to track whether an earmarked tax is sufficient to fund a program, and calling the current approach a "trust" fund is terribly misleading. For example, the Social Security program could be operated without a trust fund, and it would have exactly the same economic impact and the same effect on the unified deficit. Yet, when people see that a trust fund has considerable assets, they may conclude that the related program is financially healthy, even though the assets do not come close to financing future obligations.

Federal trust funds differ significantly from private-sector trust funds. For example, claims against a private trust fund are limited by the value of the fund's assets. By contrast, federal trust funds function as accounting mechanisms that record tax receipts, user fees, and other credits and associated expenditures. When trust fund receipts exceed expenditures, the

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<sup>6</sup> For more information, see "Evaluating and Accounting for Federal Investment in Corporate Stocks and Other Private Securities." CBO. 2003.

<sup>7</sup> "Federal Trust and Other Earmarked Funds: Answers to Frequently Asked Questions." GAO. 2001.

government's books show trust fund balances growing. However, those balances are claims on the Treasury that, when redeemed, will have to be financed by raising taxes borrowing from the public, or reducing benefits or other expenditures.

Further, the beneficiary of a private trust fund usually owns the fund's income and often owns its assets. The trustees of the fund also have a fiduciary responsibility to manage the fund on behalf of its beneficiaries and cannot make unilateral changes to the provisions governing the trust. In contrast, federal trust funds are generally owned by the federal government. They are created by law, and lawmakers can change those laws or repeal them.

Those and other distinctions between federal and private trust funds create confusion among lawmakers and the public and cause some to argue that the spending and revenues credited to federal trust funds should be treated differently in the budget process and, as noted above, be completely off budget. That argument puts pressure on lawmakers to favor those trust funds in their annual budgetary deliberations and potentially limits their flexibility in setting broad budget policies and priorities. Trust revolving funds can create yet another source of confusion when they are established as a mechanism to disguise the use of offsetting receipts to fund spending directly without going through the appropriation process.

*Capital Investments.* It is obvious that capital investments by the government have a very different impact on the economy than do current expenditures. Assuming that the investments are well allocated, they add to productivity growth and improvements in living standards in the long-run. Current expenditures may have immediate benefits but little effect on the long run. Therefore, many advocate that the budget should treat capital outlays differently from current expenditures. A presidential commission considered this topic several years ago and recommended against having a formal capital budget because of the problem of defining "capital" and the worry that the definition of capital would expand rapidly if it were deemed permissible to deficit finance "capital" spending.<sup>8</sup> A new Commission on Budget Concepts should revisit this important topic and decide whether it agrees with the previous capital budgeting commission.

*Loans and Guarantees.* Subsidized direct loans by government and loan guarantees had very different impacts on the federal deficit under the accounting practices used before 1990, even though the two types of programs had very similar economic impacts. Direct loans increased the deficit significantly in the short run and decreased it in the long run when loans were repaid. Guarantees tended to increase the deficit in the long run and might reduce deficits in the short run if a guarantee fee was levied. The Credit Reform Act of 1990 put the two types of credit assistance on an equal basis by requiring that present value accounting be used to compute the value of subsidies inherent in both types of programs. Although this was a positive change, questions have arisen over whether the estimating procedures could be improved. For

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<sup>8</sup> "Report of The President's Commission to Study Capital Budgeting", US Government Printing Office, September 30, 1999.

example, there is considerable controversy over the discount rate that should be used in estimating present values. In particular, should the discount rate add a risk premium when repayments are uncertain?

There is an off-budget account that finances the cash flows related to credit programs.<sup>9</sup> If it is depleted, it is an indication that OMB has been underestimating the cost of credit programs. Any deficit is covered by an automatic indefinite appropriation. But is this appropriate? Or should Congress have to explicitly recognize a deficit by voting on an appropriation bill?

It has often been suggested that accrual concepts be expanded to cover other areas of the budget. Insurance programs are similar to credit programs in many respects, although for some it would be extremely difficult to estimate present values.

*Macroeconomic Impacts.* Recently, congressional rules have been amended to require an analysis of the macroeconomic impacts of major tax and spending proposals (e.g., “dynamic scoring”). A new Commission might consider the methods that should be used and how the results might be displayed in the budget.

Question #2:

During the hearing, you discuss the budget enforcement mechanisms of both Sweden and Australia.

You mention that Sweden has twenty-seven budget categories. What criteria or methodology did Sweden use to organize these categories?

How does Australia build long-term projections and planning into their budget projections?

How do other nations set their spending limits? Do they use a formula? Do elected leaders set the limits?

How have other countries structured their enforcement mechanisms? If it's a sequestration, what portions on the budget are automatically reduced?

Response:

My responses to these questions are divided into three sections for Sweden, Australia, and other nations.

*Sweden*<sup>10</sup>

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<sup>9</sup> Technically, the account is not said to be off budget. Rather it is “below the line” in that its deficit does not affect the computation of the unified budget deficit.

<sup>10</sup> This response is largely taken from “Budgeting in Sweden”, by Jon R. Blondal, *OECD Journal on Budgeting*, Organization on Economic Cooperation and Development, Paris, Vol. 1, No. 1, 2001.

From enjoying the largest budget surpluses of any OECD Member country in the late 1980s, Sweden went into having the largest budget deficits of any OECD Member country in the early 1990s, which were accompanied by a massive increase in government debt. In a span of just five years, the level of debt had nearly doubled. However, by the late 1990s, the budget had been brought back to balance. The government believed that the budget process itself had contributed significantly to the deterioration of the public finances.

The key elements of the reforms included the adoption of a multi-year budget framework and a top-down budget process. A Spring Fiscal Policy Bill was introduced whereby Parliament discusses and approves the key aggregate figures in the budget framework. The budget process was made more comprehensive by the inclusion of entities that had previously operated off-budget, primarily in the social security field. The principle of gross budgeting (separating revenues and expenditures) was adopted to increase transparency for certain transactions, again primarily in the social security field. This principle was, however, not applied to user charges for government service where its application was seen as a disincentive for levying user charges. **All open-ended permanent appropriations were abolished and became subject to annual scrutiny and authorization. This applied primarily to various entitlement programs.** Furthermore, the fiscal year was changed to the calendar year (which started previously in July) and the legal basis for budgeting was strengthened. This involved the enactment of a State Budget Act and additional measures in Parliament's standing orders in relation to the budget process. In practice, this often meant codifying practices that had previously been subject to administrative decision or simply tradition.

There are about 500 appropriations in the Swedish budget. There are separate appropriations for operating costs, transfer programs and capital outlays. A majority of the appropriations are for operating costs, mainly for the operations of agencies. An innovation in their budget reforms was to group all government appropriations into 27 Expenditure Areas. (See the listing of these Areas below.) This is the basis on which the Spring Fiscal Policy Bill and the Budget Bill is presented to Parliament. Previously, the appropriations were divided by the ministries responsible for the appropriations. **The 27 Expenditure Areas were proposed by Parliament, which wanted a clearer presentation of expenditures on individual policy areas than was afforded by the division by ministry. It was also designed to reflect the committee structure in Parliament.** As there are 13 ministries in Sweden, a minister can be responsible for more than one Expenditure Area. There are also instances of two or more ministers being responsible for a single Expenditure Area. In such cases, the responsibility for each appropriation within the Expenditure Area is assigned to the respective minister. Despite this apparent complexity, Swedish officials emphasized that this presentation is working very well.

Sweden employs a multi-year budget framework as the basis for the annual budget process. It has a three-year time horizon, i.e. the upcoming budget and the two following years. The multi-year budget framework provides the link between the government's fiscal policy objectives in a macroeconomic context and their application in an operational context. It operates on three

cascading levels. The first level constitutes the articulation of the government's fiscal policy objectives in macroeconomic terms, i.e. level of surplus or deficit as a percentage of GDP. At the second level, these objectives are translated into a maximum level of total expenditure based on certain economic assumptions. At the third level, the limit for total expenditure is further operationalized by giving indicative funding levels for each of 27 Expenditure Areas.

The multi-year budget framework is legally binding. Parliament approves the maximum level of total expenditure for the government (Level 2) and the indicative level of funding for each of the 27 Expenditure Areas (Level 3). The limits are stated in nominal terms. The total for the indicative level of funding for the 27 Expenditure Areas is less than the maximum level of total expenditure. This difference constitutes the "budget margin". For example, the budget margin might be 1.5% in Year 1; 2% in Year 2; and 2.5% in Year 3. The purpose of the budget margin is to provide a buffer against any forecasting errors so that the maximum level of total expenditure approved by Parliament would not have to be amended.

**It must be emphasized that all the above decisions are made at the level of the Expenditure Areas, not at the level of each appropriation. It is only in the last phase of the budget formulation process that decisions on each appropriation are made. These decisions are made by the ministers responsible for each Expenditure Area. "Each minister is his own Finance Minister" within the limits set for his Expenditure Area.** The Ministry of Finance largely withdraws from the budget formulation process during this phase. This has given the spending ministers greater ownership over their respective budget proposals and made them more likely to identify lower priority programs within their Expenditure Areas to finance higher priority initiatives.

**OECD concluded that the "budget process has shown itself to be quite effective in maintaining aggregate fiscal discipline."**<sup>11</sup> Allocative efficiency in the budget process is fostered. Supplementary budgets are presented to Parliament twice a year – in April coinciding with the Spring Fiscal Policy Bill and in September coinciding with the Budget Bill. Increased funding for transfer programs, notably unemployment benefits and specific transfers to municipal and county governments have been the major components of the supplementary budgets. **Increased funding for these areas has been financed by reductions in other Expenditure Areas and by increases in revenue (consistent with the budget margin) by the decentralized nature of the final allocation of funds to appropriations within each Expenditure Areas.** It would, however, appear to be hampered by the very limited time frame that Cabinet has to agree to allocations among the 27 Expenditure Areas.

The budget process that Parliament has adopted is comprehensive and disciplined. It is marked by an acceptance of Parliament to heed to a set of binding budgetary constraints when discussing the budget. In addition, the number of amendments approved in Parliament to the

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<sup>11</sup> *Ibid.*, p. 36.

government's budget proposal has decreased significantly following the adoption of the new budget process.

#### List of Sweden's 27 Expenditure Areas

1. The Swedish Political System.
2. Economy and Fiscal Administration.
3. Tax Administration and Collection.
4. Justice.
5. Foreign Policy Administration and International Co-operation.
6. Defense.
7. International Development Assistance.
8. Immigration and Refugees.
9. Health Care, Medical Care, Social Services.
10. Sickness and Disability Benefits.
11. Old-Age Benefits.
12. Family and Children's Benefits.
13. Unemployment Benefits.
14. Labor Market.
15. Study Support.
16. Education and University Research.
17. Culture, the Media, Religious Organizations, Leisure.
18. Planning, Housing Supply, Construction.
19. Regional Development.
20. General Environment and Development.
21. Energy.
22. Communications.
23. Agriculture, Forestry, Fisheries.
24. Business Sector.
25. General Grants to Municipalities.
26. Interest on Debt.
27. Contribution to European Union Budget.

#### *Australia*<sup>12</sup>

The budget process in Australia has undergone profound reforms during the past quarter of a century and can be said to have been in a state of continual change/reform since the launch of

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<sup>12</sup> This response is largely taken from "Budgeting in Australia", by Jon R. Blondal, Daniel Bergvall, Ian Hawkesworth, and Rex Deighton-Smith, *OECD Journal on Budgeting*, Organization on Economic Cooperation and Development, Paris, Vol. 8, No. 2, 2008.

a White Paper entitled “Budget Reform” in 1984, which set the process in motion. Early reforms focused on reducing central input controls and granting more flexibility to spending ministries and agencies. Line items were systematically merged through the running costs arrangements; subsequently, centralized manpower controls were abolished, and the budget was the only constraint on staffing levels. There was a complementary system of carry-overs of unused running cost appropriations to the next fiscal year. These constituted the principal elements of the Financial Management Improvement Program. A medium-term expenditure framework (the forward estimates) and a more effective cabinet committee process for identifying priorities and promoting fiscal discipline were launched. The reforms aimed to increase the focus on performance and results, originally starting with program budgeting and a formal system of program evaluations. This focus was the quid pro quo for increased flexibility.

The reforms also coincided with the introduction of the Charter of Budget Honesty Act (the Charter), which legislated a high level of budget transparency and specific disclosures. The Charter was intended to help entrench sound and transparent fiscal policies and make it difficult for future governments to deviate from them. The Charter provides a comprehensive legal framework for the formulation and conduct of fiscal policy in general. The provisions of the Charter can be divided into two groups: a regime for setting fiscal objectives, and an extensive system of fiscal reporting to monitor the consistency of the government’s fiscal actions with its stated fiscal objectives.

Setting fiscal objectives is a two-step process involving certain legislated “Principles of Sound Fiscal Management” and an annual “Fiscal Strategy Statement” prepared by the government.

The Principles of Sound Fiscal Management require the government:

- To manage financial risks faced by the Commonwealth prudently, having regard to economic circumstances, including by maintaining Commonwealth general government debt at prudent levels.
- **To ensure that its fiscal policy contributes to achieving adequate national savings and to moderating cyclical fluctuations in economic activity, as appropriate, taking account of the economic risks facing the nation and the impact of those risks on the government’s fiscal position.**
- To pursue spending and taxing policies that are consistent with a reasonable degree of stability and predictability in the level of the tax burden.
- To maintain the integrity of the tax system.
- **To ensure that its policy decisions have regard to their financial effects on future generations.**

These Principles of Sound Fiscal Management are translated into specific government objectives through an annual Fiscal Strategy Statement. The Statement in turn provides a benchmark for evaluating the government’s fiscal policy performance. In the Fiscal Strategy



Statement, which is published as part of the budget documentation, the government is required by the Charter to:

- **specify the government’s long-term fiscal objectives within which shorter-term fiscal policy will be framed;**
- specify the key fiscal measures that the government considers important and against which fiscal policy will be set and assessed;
- specify for the budget year and the following three financial years the government’s fiscal objectives and targets and the expected outcomes for the specified key fiscal measures;
- explain how the fiscal objectives and strategic priorities specified relate to the principles of sound fiscal management;
- specify fiscal policy actions taken or to be taken by the government that are temporary in nature, adopted for the purpose of moderating cyclical fluctuations in economic activity, and indicate the process for their reversal.

The fiscal objectives are stated in general terms in the legislation and do not mandate any specific fiscal targets, but rather refer to “prudent levels” and “reasonable degrees”. It is left to the government of the day to specify its interpretation of the relevant fiscal terms in the Fiscal Strategy Statement.

The Charter specifically allows the government to temporarily depart from the general principles of responsible fiscal management. In doing so, the government must indicate the process for the reversal of such measures.

**In cases of non-compliance, the Charter does not call for legal penalties. It does, however, mandate the production of a comprehensive set of reports in order to monitor the consistency of the government’s fiscal actions against its stated fiscal objectives. The objective is to ensure that the “court of public opinion”, not a law court, is able to make the necessary judgments on the government’s fiscal management.**

The reports are the Economic and Fiscal Outlook released at the time of the budget, the Mid-Year Economic and Fiscal Outlook released approximately six months after the budget, and the Final Budget Outcome Report released three months after the end of the fiscal year. In addition, the Charter requires a Pre-Election Economic and Fiscal Outlook to be presented within ten days of an election being called. **An Intergenerational Report, designed to assess the long-term sustainability of current government policies, must be produced at least every five years.**

The Intergenerational Report focuses on the implications of demographic changes for economic growth and assesses the financial implications of continuing current policies and trends over the next four decades (two generations). The report outlines the government’s fiscal sustainability objectives and its approach to achieving them, and gives details on Australia’s

long-term demographic and economic projections. Based on the projections, the report provides detailed estimates for future revenue and spending projections and the resulting budget balance. The report contains sensitivity analysis of the projections and goes into detail on the methodology and assumptions used.

**The reports attract much public and media attention.** The five-year interval allows a narrative to be written of policy changes in the intervening period and of their impact on fiscal sustainability. This time-frame also coincides with Australia's five-yearly population census. Although demographics may change slowly, annual fiscal policy decisions can and frequently do affect the long-term outlook every year.

As stated in the most recent report, "The Intergenerational Report is the social compact between generations – with our children, grandchildren, parents, grandparents and each other."<sup>13</sup>

#### *Other Nations*

The elected leaders of other nations set limits, informed by various sources, but not based on formulas per se. The United States is the only country to utilize a formal sequestration mechanism. However, the separation of powers among the branches of U.S. government and the power of the U.S. legislature over the budget are much stronger than in any other OECD country.

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<sup>13</sup> 2015 Intergenerational Report: Australia in 2055, Australian Government, 2015, p. 6.

#### Questions from Senator Stabenow

You discussed both the importance of long-term budget projections and the need to improve the presentation of that data. There is significant uncertainty in long-term spending and revenue projections, and small differences in the underlying assumptions can lead to widely different projections.

Drawing on your experience as both a senior official at OMB and as Acting Director of CBO, is there more that both offices could be doing to make their analyses more clear and long-term projections easier to compare?

#### Response:

I am a long-time Board member of the Committee for a Responsible Federal Budget (CRFB), a bipartisan, non-profit organization made up of some of the nation's leading budget experts including many past Chairmen and Members of the Budget Committees and the Federal Reserve Board, and Directors of the Congressional Budget Office, the Office of Management and Budget, and the Government Accountability Office. The excellent analysis of the CRFB staff highlights that the unsustainable U. S. long-term fiscal outlook is driven almost exclusively by four sources: Medicare, Medicaid, Social Security, and tax expenditures.

Thus, OMB and CBO should increase the attention they place on identifying these four "drivers" as the causes of our unsustainable fiscal future, on detailing the reasons behind their projections, and on explaining how relatively sensitive their projections are to certain economic, demographic, and other technical factors.

A primary example of where this increased attention should be placed is health care costs. Long-term projections of national health care expenditures, which include but are not limited to federal outlays on health care, have been produced for many years by the Department of Health and Human Services' Center for Medicare and Medicaid Services (CMS). As these projections take into account the full range of health care in the U. S., and thus the shifts between public and private financing of health care, changes in the use of in- and out-patient treatments, changes in insured and un-insured populations, changes in the use of health care influenced by short-term economic downturns and those reflecting longer-term patterns of

usage, and other important factors, they provide an extremely valuable source for OMB and CBO on which to base their long-term projections of federal health care outlays. As the table below shows, over the past six years the CMS projections of *current* national health care expenditures have varied from a low of 17.2% of GDP (the 2010 and 2014 projections for 2012) to as much as 19.0% (the 2015 projection for 2015). But despite all the changes and fluctuations during the past six years, CMS's *long-term (10-year) projections* have not dropped below 19.3% and are currently at 19.6%, higher than the 10-year projections made in 2010. OMB and CBO should use this data as the basis for their projections over periods beyond 10 years and carefully explain the factors in the CMS projections that they rate as most important.

### US National Health Expenditures as a % of GDP

Source: Sean Keenan, et al., of HHS's Center for Medicare & Medicaid Service, "National Health Expenditure Projections", *Health Affairs*, 2010-13.

Calendar Years	2010 Projection Before ACA	2011 Projection After ACA	2012 Projection After ACA	2013 Projection After ACA	2014 Projection After ACA	2015 Projection After ACA
2009	17.3	17.6	17.9	17.9	--	--
2010	17.3	17.6	17.9	17.9	--	--
2011	17.3	17.7	17.9	17.9	--	--
2012	17.2	17.6	17.9	17.9	17.2	17.4
2013	17.3	17.6	17.8	18.0	17.2	17.4
2014	17.4	18.1	18.2	18.3	17.6	17.7
2015	--	--	--	18.4	17.6	19.0
2018	--	--	--	18.5	--	18.1
2019	19.3	--	--	--	18.1	--
2020	--	19.8	--	--	--	--
2021	--	--	19.6	--	--	--
2022	--	--	--	19.9	--	--
2023	--	--	--	--	19.3	--
2024	--	--	--	--	--	19.6

### Questions from Senator Whitehouse

#### Question #1:

Would you support limiting the number of votes during the Senate's consideration of the budget resolution to avoid a "vote-a-rama," which is often filled with mischievous nonsense? If we implemented such a reform, do you believe that it would increase the chances the senate would pass a budget resolution in any given year?

#### Response:

Yes to both. As my career has been primarily in the executive branch (OMB for 18 years), legislative support agencies (CBO and GAO for 12 years), international budgeting (IMF and OECD for 7 years), and budgeting in the states (NGA for 5 years), I have only observed vote-a-ramas from afar. Nevertheless, I believe that any process change that would encourage the Congress and the president to come together to produce a joint budget would be helpful.

#### Question #2:

Would you support greater transparency in the budget resolution, so that proposed budget levels are connected to actual accounts?

#### Response:

Yes. The more transparency and detail in the resolution, the better the chance that the Congress and the president have the data to help them resolve their policy differences.

#### Questions #3:

What would you think about the Budget Committee setting a goal for an appropriate debt-to-GDP ratio and proposing a glide path to achieve it over a number of years? What kind of entitlement "fences" could be used to ensure Congress stays within the glide path? In evaluating potential enforcement mechanisms, do you agree that Congress must consider tax expenditures along with direct spending?

Response:

The research that I did while at OECD strongly supports that establishing multi-year debt-to-GDP goals, and then achieving those goals through enforceable caps on spending—to include discretionary and entitlement spending and tax expenditures—is the best system to promote economic growth through a long-term sustainable fiscal plan.<sup>14</sup> I would note that there are already caps of a fashion on some tax expenditures. That is, both the alternative minimum tax and the “Pease Limitation” on the deductibility of certain itemized deductions limits the use of some—but clearly not all-tax expenditures.

The results of my research on the best fiscal policy rules are summarized below.<sup>15</sup>

Both in abstract analysis and in the practical record, there seems to be little identifiable advantage in the use of deficit rules for fiscal behavior. If anything, the balance would seem to lean toward **spending rules that are simpler and less prone to malfeasance.**

- With respect to fiscal responsibility, deficit-based rules that set only (in effect) a maximum limit on the deficit might be thought to encourage countries to run the largest deficits permitted, creating risks of excessive deficits under unexpected adverse conditions. In contrast, a spending rule would provide firm guidance to policy makers whether the economy and the budget are strong or weak.
- With respect to macroeconomic stabilization, **deficit-based rules provide no incentive for counter-cyclical policy in strong economies**, and can limit even the operation of automatic stabilizers in the budget in weak economies. In contrast, **spending rules allow the automatic stabilizers to work in full at all times and in any economic conditions.**
- Violations of a spending rule are transparent and incontrovertible. In contrast, non-compliance with a deficit rule, including either a reference deficit limit or required progress toward close-to-balance or in-surplus status, can be hidden behind optimistic economic assumptions or unlikely plans for future spending and revenue discipline.
- The performance of the core functions of government – its ability to achieve all of the traditional objectives of the public sector – can be adversely affected if the availability of resources is subject to unpredictable decreases or increases based only upon cyclical developments, as can be the case under deficit rules. Spending rules make the availability of resources more predictable, notably with respect to annually appropriated funding for those core functions of government.
- Funding for public investment can be protected under a spending rule, by requiring additional fiscal restraint through mandatory spending or taxes, or by setting a separate appropriations limit for investment.

<sup>14</sup> “Design Choices for Fiscal Policy Rules”, by Barry Anderson and Joe Minarik, *OECD Journal on Budgeting*, Organization on Economic Cooperation and Development, Paris, Vol. 5, No. 4, 2006.

<sup>15</sup> The OECD article on fiscal policy rules also highlights and provides detail on the success of the spending rules implemented by Finland, the Netherlands, and Sweden.

- In contrast to the unpredictable fiscal constraints imposed by deficit rules, the more predictable fiscal behavior encouraged by spending rules can lead to easier coordination with monetary policy, and to greater confidence and steadier behavior within the private sector.

“Better Budgets, Better Results”  
Senate Budget Committee Hearing  
April 27, 2016

Responses to Questions for the Record

James C. Capretta  
Senior Fellow, Ethics and Public Policy Center,  
Visiting Fellow, American Enterprise Institute, and  
Affiliated Scholar, Mercatus Center at George Mason University

**Questions from Chairman Enzi**

Question #1:

Some critics of a joint budget resolution have pointed out that one branch or the other could use the budget as a political tool to highlight policy differences, which would lead to a breakdown in the budget process. You have argued that in the event a Joint Resolution Budget is vetoed, Congress could maintain the options for a Concurrent Resolution on the Budget.

Would this mitigate the use of the budget as a political weapon?

Is there a risk that this reversion mechanism would undermine the pressure to pass a joint budget resolution, allowing a concurrent resolution to remain the norm?

Answer:

It is certainly possible that Congress may want to send a joint budget resolution to the president with the expectation that it would be vetoed. That happens sometimes already with other legislation. If that were to happen with a joint budget resolution, perhaps there would be greater clarity about the differing views of the branches that could then be debated in an election.

But it seems just as likely that creating the opportunity for a joint budget resolution will create some pressure on both branches to compromise. Not many bills actually get vetoed because it is not easy to get a bill to the president’s desk and so legislators generally want their efforts to result in new laws, not vetoes. At the same time, presidents are reluctant to veto bills unless they can clearly explain their objections in ways that are persuasive for voters.

The recommendation that Congress be allowed to revert to a concurrent resolution in the event a joint budget resolution is not agreed is a recognition of reality. There will be times when Congress and the president cannot agree early in the year, and a concurrent resolution will allow Congress to proceed with bills as it does today.



Question #2:

Throughout the years Congress has relied on Continuing Resolutions when the appropriations process breaks down. As we look to reform the budget process, what are some steps that Congress could take to incentivize passing appropriations under the regular order?

Answer:

Sen. Rob Portman has proposed an automatic CR process that I believe deserves consideration. An automatic CR is a permanent law that provides funding to agencies and programs that rely on discretionary appropriations in the event an appropriations bill is not enacted. The amount of funding is tied to the funding level from the prior year, perhaps with a small reduction to ensure pressure mounts to pass a regular funding bill. The amount of the reduction could increase as time passed to increase the pressure on Congress to pass a regular appropriations bill. Automatic CRs would ensure there would not be a government shutdown if the two branches could not agree on a full-year appropriations bill.

Question #3:

One weakness of our current budget system is that it has a tendency to focus on the short-term, while many of our greatest fiscal challenges exist in the long-term. You have described potential steps to place a stronger emphasis on long-term budget considerations.

Why is greater emphasis on the long-term important for making the budget more meaningful?

As we examine the role of long-term concerns in the budget, how would you advise this committee given the heightened uncertainty of long-term projections?

Answer:

The federal government is running relatively large budget deficits today, but the primary problem is the expected run-up in debt over the medium and long-term, due to rising spending on entitlement programs. The large unfunded liabilities of these entitlements creates significant economic uncertainty, thus lessening productive investment and growth in the U.S. economy.

It will not be possible to make abrupt changes in spending on most of these programs because so many millions of beneficiaries are dependent on them for health care and income security. Adjustments in these programs need to take place over many years, which means they need to be enacted now to provide enough time for an adequate transition period. The federal budget would be in much better shape today if serious entitlement reforms had been enacted 15 or 20 years ago.

The current budget process does not present policymakers with clear information about the long-term challenge, or provide a realistic pathway for legislation addressing it. That is an important defect that needs to be corrected.

While it is true that there is some uncertainty around long-term projections, the direction of entitlement spending is clear enough. Demographic trends and rising health care spending will push spending up rapidly in the coming years, creating significant budgetary pressure. The magnitude of the rise in spending may differ somewhat from current projections, but the likelihood that the entire problem will simply go away due to slower than expected spending growth is very low.

#### **Questions from Senator Whitehouse**

##### Question #1:

Would you support limiting the number of votes during the Senate's consideration of the budget resolution to avoid a "vote-a-rama," which is often filled with mischief and nonsense? If we implemented such a reform, do you believe that it would increase the chances the Senate would pass a budget resolution in any given year?

##### Answer:

I support reforms to the current process that would eliminate entirely non-substantive changes to the budget resolution. Most of the votes on a budget resolution come in the form of "Sense of the Senate" amendments that are not binding and do not in any way change the key budgetary limits of the resolution. Eliminating amendments of this kind would go a long way toward relieving the Senate of the "vote-a-rama" ordeal every year.

##### Question #2:

Would you support greater transparency in the budget resolution, so that proposed budget levels are connected to actual outcomes?

##### Answer:

I support more transparency in the entire budget process. The budget resolution is mainly a forward-looking plan, and so it necessarily uses projections, not actual spending and revenue numbers. Nonetheless, it may be possible to include in the resolution more actual numbers from recent fiscal years to inject a dose of reality into the document. I would support that.

##### Question #3:

What would you think about the Budget Committee setting a goal for an appropriate debt-to-GDP ratio and proposing a glide path to achieve it over a number of years? What kinds

of enforcement “fences” could be used to ensure Congress stays on the glide path? In evaluating potential enforcement mechanisms, do you agree that Congress must consider tax expenditures along with direct spending?

Answer:

I think the Committee should looking out to the medium term – around 10 to 15 years from now – and setting goals for revenue, spending, and debt. The Committee should then work through a list of ideas of how to reform the major programs to hit those goals, with long transitions and a glide path.

In terms of enforcement, I favor broadening and strengthening the sequester process to cover much more entitlement spending. I would be open to inclusion of some targeted tax expenditures in a reformed approach to enforcement f that were helpful to getting bipartisan support for it.

**Stan Collender's Responses to Questions for the Record from Sen. Whitehouse****Question:**

Would you support limiting the number of votes during the Senate's consideration of the budget resolution to avoid a "vote-a-rama," which is often filled with mischief and nonsense? If we implemented such a reform, do you believe that it would increase the chances the Senate would pass a budget resolution in any given year?

**Response:**

Eliminating "vote-a-rama" will do nothing to increase the chances the Senate will pass a budget each year. Budgeting is the most political of all processes and politics cannot be eliminated no matter how much you might like to do so. Take away vote-a-rama and something else will develop that will enable senators to sound like they are representing their voters or supporters.

**Question:**

Would you support greater transparency in the budget resolution, so that proposed budget levels are connected to actual accounts?

**Response:**

Budget resolutions were deliberately made less transparent in the Congressional Budget and Impoundment Control Act to protect the jurisdiction of the tax-writing and spending committees. These committees felt that they would no longer have as much power if the budget resolutions were more specific and their choices limited. Without their support, the Congressional Budget and Impoundment Control Act would not have had enough votes to pass. Unless Congress is willing not just to re-litigate this issue but to rule against the House and Senate Appropriations, House Ways and Means and Senate Finance Committees, the lack of transparency will always remain.

**Question:**

What would you think about the Budget Committee setting a goal for an appropriate debt-to-GDP ratio and proposing a glide path to achieve it over a number of years? What kinds of enforcement "fences" could be used to ensure Congress stays on the glide path? In evaluation potential enforcement mechanisms, do you agree that Congress must consider tax expenditures along with direct spending?

**Response:**

Multi-year federal budgets and glide paths are worthless because, except by accident, they prevent budgets that are relevant to the current needs of the economy. Setting goals is fine, but locking the federal budget into a multi-year fiscal policy is economic malpractice.

Yes, tax expenditures and direct spending should always be part of the budget debate.

**Stan Collender's Response to Question for the Record from Sen. Stabenow****Question:**

Mr. Collender, you state in your testimony that this Committee and the Congress as a whole are to blame for the breakdown of the budget process.

Given the current environment and unfortunate lack of bipartisanship we are faced with, what specific steps or changes would you suggest we implement to create, to quote your testimony, "a consensus about what the budget process should do"?

**Response:**

There's no way today to create a bipartisan and generally accepted consensus about what the congressional budget process should do. As I said in my testimony: Changing the budget process now...or even anytime soon...shouldn't be tried.

Past budget processes have always developed in response to political crises. In 1974, the Congressional Budget and Impoundment Control Act was adopted after two years of discussion, special committees and votes in the House and Senate. But it never would have been agreed to had President Nixon not refused to spend enacted appropriations as required, that is, to impound. Congress realized that it didn't have a way to respond to the president's intransigence so it created a process to do that. The other budget procedures might still be languishing in committee had there not been this extreme political consternation.

The same was true in 1985 of the Balanced Budget and Emergency Deficit Control Act or, as it's better known, Gramm-Rudman-Hollings. In that case the crisis was the politically created perception that the budget deficit absolutely had to be reduced. That led to a new process that, unlike the Congressional Budget and Impoundment Control Act, mandated annual deficit reductions.

Given the number and type of catastrophes we've had in this country the past few years --we clearly have what I call "crisis fatigue"--I hesitate even to try to imagine what type and how serious a crisis we will need today to create the environment that would allow a new budget consensus and budget process to be adopted.

## OVERSIGHT OF THE CONGRESSIONAL BUDGET OFFICE

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WEDNESDAY, SEPTEMBER 14, 2016

U.S. SENATE,  
COMMITTEE ON THE BUDGET,  
*Washington, D.C.*

The Committee met, pursuant to notice, at 3:31 p.m., in Room SD-608, Dirksen Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Toomey, Johnson, Perdue, Whitehouse, and King.

Staff Present: Matthew Giroux, Deputy Staff Director for the Majority; for the Minority: Joshua Smith, Budget Policy Director.

### OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. I will go ahead and call this hearing to order. I am not expecting a huge turnout.

Last year, the Senate Budget Committee conducted its first hearing in more than 30 years to provide oversight for the Congressional Budget Office. At that hearing I announced that we were resetting our oversight relationship with the CBO and we would faithfully execute Section 102(a) of the Congressional Budget Act. This provision gives the Senate Budget Committee the duty to review on a continuing basis the conduct of the Congressional Budget Office and its functions and duties.

When our last oversight hearing was held, Dr. Hall was on the job as CBO's Director for less than 2 full months, so it probably was not fair to have it then. But, again, I was trying to follow the law. Dr. Hall has now been at the helm for over a year and has seen CBO through an entire Federal budget cycle. This means he has been able to oversee CBO's work on its recurring projections, thousands of formal and informal estimates of legislation, and then special reports requested by Members of both the House and the Senate.

In conducting the day-to-day operations of this Committee, I find CBO reports and estimates to be of great assistance, particularly in my role as the Senate scorekeeper on budgetary issues. I look forward to hearing what experience you have had thus far and the goals you have for CBO under your leadership to continue the agency's reputation for providing objective and insightful information to Congress.

We on the Committee as interested in where things stand with the goals you identified from our last hearing. We are particularly interested in your efforts meant to increase transparency of CBO's

analysis and operations, which you stated was one of your primary objectives.

During our most recent work period, CBO released its latest round of projections this year, the update to the Budget and Economic Outlook: 2016 to 2026. What this report heralded was not a surprise to anyone. Whether under the leadership of Dr. Hall or his predecessor, CBO has continually showed in recent years that we are on the wrong fiscal track, and America's current budget path is simply unsustainable.

We have been having some hearings on that throughout the year to see what sorts of things could be done to change it. We have a list that there seems to be some agreement across the aisle on that could make a huge difference for America. But the August report has revealed that this fiscal year we will overspend by \$590 billion. That is up \$152 billion from last year's deficit.

There is no end in sight to this overspending. CBO tells us the deficits will hit the \$1 trillion mark or, to say it differently, \$1,000 billion mark in 2024 and continue their upward trajectory. By the end of CBO's projection window, 2026, our Nation's mammoth debt will reach more than \$28 trillion, or nearly a 50-percent increase from today's level. Clearly, we have a problem.

This Committee has spent the year holding numerous hearings and evaluating ways to fix our broken budget process. That work continues, but it is clear to me that when we are finally able to get this process back on track, CBO will be a critical element in getting our fiscal house in order. Its independence and nonpartisanship will be essential to get both sides of the aisle together to confront our budget realities. As such, the Committee remains invested in ensuring CBO has the policies, practices, and personnel in place to continue to fulfill its core mission of providing Congress the information it needs to make knowledgeable budget and economic policy.

As part of the Committee's ongoing efforts to make sure CBO is able to continue supplying Congress with accurate information in the most complete way possible, I was proud to include several provisions in the last budget resolution to require CBO to take into account the real-world effects that legislation would have on our budget. Most notably, Section 3112 of S. Con. Res. 11, the concurrent resolution on the budget for fiscal year 2016, which requires CBO to estimate the macroeconomic effects of major policy changes. This has come to be known as "dynamic scoring," but in my view, it should be known as "honest accounting," and that should be our goal.

Now that CBO has had several opportunities to conduct this macroeconomic analysis, the Committee is interested in hearing what you have learned about this approach, what you view as the next steps in integrating this approach into CBO's operations, and how you plan to maintain transparency with your methodologies. Just as CBO will continue to be a crucial component in the Federal budget process, so, too, must this Committee's oversight of CBO. I look forward to fostering this constructive relationship, both in today's hearing and in the future.

Would you like to make any statement?



Senator KING. Mr. Chairman, I was looking forward to Dr. Hall's testimony, and I will have some questions. Thank you.

Chairman ENZI. Okay. And if Senator Sanders or Senator Whitehouse come, we will give them time for a statement as well. But especially since we are starting late, I want to continue on so that we do not take more of your valuable time.

I would imagine that everybody here knows exactly who Dr. Hall is, or they probably would not be here. But at any rate, he is the ninth Director of the Congressional Budget Office. He is no stranger to this Committee, having served as CBO Director since April of last year. Since that time he has appeared before this Committee to discuss CBO's work as a congressional support agency and its projections of the Nation's ever-worsening fiscal situation. Dr. Hall has over 25 years of experience in various Government positions, including serving as the Chief Economist and Director of Economics at the International Trade Commission. He was the Chief Economist for the White House Council of Economic Advisers, and he was Chief Economist for the Department of Commerce. He has held several academic posts. He has earned his Ph.D. and M.S. in economics from Purdue University.

This afternoon, Dr. Hall will be talking with us about CBO's work over the last year and the goals he has set out for his critically important agency, and we look forward to receiving your testimony.

With that, Dr. Hall, I turn it over to you. Thank you for being here.

#### **STATEMENT OF KEITH HALL, DIRECTOR, CONGRESSIONAL BUDGET OFFICE**

Mr. HALL. Chairman Enzi and Members of the Committee, I appreciate the opportunity to discuss the work of the Congressional Budget Office. CBO's mission is an important one: to provide non-partisan budgetary and economic analysis that is timely and carefully thought out in order to support the work of the Committee and the Congress as a whole as you address the critical issues facing the Nation.

To that end, CBO is committed to providing information that is: objective, representing the consensus and diversity of views of experts from around the country; insightful, applying the best new evidence and innovative ideas as well as the lessons of experience; timely, responding as quickly as possible to the needs of Congress; and clearly presented and explained so that policymakers and analysts understand the basics of our findings and have the opportunity to question the analysis and methods used.

All of CBO's estimates and reports are reviewed internally for objectivity, analytical soundness, and clarity. And in releasing our results, we are committed to maintaining a level playing field, ensuring that our work is made widely available to Congress and the public.

Just as the Budget Committees rely on us for sound and timely advice, we rely on you as well to explain and communicate to others in the Congress what CBO's role is, to provide constructive feedback on how we can best serve the Congress, and to provide guidance on what legislative developments are occurring and what

the Congress' priorities are. We are very grateful for that support and guidance, which are key to our success.

Since I last testified about CBO's work before you in May 2015, we have continued to work diligently to carry out our mission, emphasizing five areas of work that are of particular interest to the Committee: preparing cost estimates for legislation, enhancing the transparency of our work, refining our methodology for dynamic analysis, developing greater capacity to analyze trade agreements, and continuing to build a high-quality staff.

First, to respond to the needs of the Budget Committees, CBO has prepared a multitude of cost estimates, both formal and informal, to support the Committee's role in budget enforcement as well as in the development of a budget resolution. Last year, we produced more than 600 formal cost estimates and mandate statements, as well as thousands of informal estimates to aid committees in crafting legislation. In 2016, the pace of our work is much the same.

Second, CBO continues to make its analysis transparent. Our publications go well beyond simply presenting results. Indeed, we work hard to explain the basics of our findings so that members of Congress, their staff, and outside analysts can understand the results and methodologies we used. For example, we supplemented some reports with working papers presenting details about our methodology. We also made a number of enhancements to the website, including displaying in one place the spread sheets that show budget and economic projections prepared in various years and displaying in another a collection of the detailed baseline projections for selected major programs.

Third, CBO has emphasized dynamic analysis. For example, in response to the requirement for certain dynamic analysis specific in the budget resolution for fiscal year 2016, CBO—in collaboration with the staff of the Joint Committee on Taxation—completed several such estimates in the past year, and we have devoted significant effort to developing and enhancing the analytical tools we need to assess the macroeconomic effects of fiscal policies. And in selected reports, CBO has provided estimates of the effects that significant changes in Federal spending and tax policies would have on the overall economy. We also solicited extensive feedback on our methods so that we could continue to refine and enhance our modeling approaches.

Fourth, CBO has devoted significant resources to analyzing trade agreements and improving our capability to model their effects. We continue to prepare to analyze potential legislation related to the Trans-Pacific Partnership, and we anticipate this will be the first time that we provide any dynamic analysis of a trade agreement.

Finally, CBO continues to devote resources to attracting and retaining talented people and developing their skills. Among the notable staffing changes, Mark Hadley became the agency's Deputy Director in June, and two new Assistant Directors—one for macroeconomic analysis and the other for tax analysis—joined the agency this year.

In focusing for the upcoming year, CBO will aim to further explain its analytical capability with an emphasis on macroeconomic analysis, health care issues, and modeling capabilities. We have al-

ready shifted some resources to bolster our work on dynamic analysis and have requested funding for additional staff to work on such analyses.

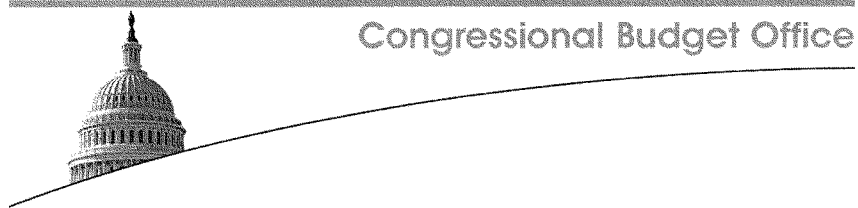
In the health area, more data will become available about the costs of expanded health insurance coverage under the Affordable Care Act, which will further our understanding of potential effects of changing that law.

We are also in the process of analyzing various aspects of our health care system and enhancing our capacity to assess the effects of future legislation on that system and on the Federal budget. To enhance the transparency of our work in this area, we will publish working papers explaining our updated and enhanced model of the health insurance system. We are also continuing to expand our capacity to analyze energy and environmental issues and to enhance our access to important sets of data.

We look forward to continuing to support this Committee as it carries out its important responsibilities by providing the Congress with budget and economic information that is objective, insightful, and timely, and by presenting and explaining the methodology and results of CBO's analyses also as clearly as possible.

Thank you for your attention. I would be happy to answer any questions.

[The prepared statement of Mr. Hall follows:]



## **Testimony**

### **The Congressional Budget Office's Work Since May 2015 and Plans for the Future**

**Keith Hall  
Director**

**Before the  
Committee on the Budget  
United States Senate**

**September 14, 2016**

*This document is embargoed until it is delivered at  
2:30 p.m. (EDT) on Wednesday, September 14, 2016.  
The contents may not be published, transmitted, or  
otherwise communicated by any print, broadcast, or  
electronic media before that time.*

Chairman Enzi, Ranking Member Sanders, and Members of the Committee, I appreciate the opportunity to discuss the work of the Congressional Budget Office. CBO's mission is an important one: to provide nonpartisan budgetary and economic analysis that is timely and carefully thought-out in order to support the work of this Committee and the Congress as a whole as you address the critical issues facing the nation. That mission constitutes my core responsibility.

We at CBO have relied on the budget committees to explain and communicate to others in the Congress what the agency's role is, to provide constructive feedback on how the agency can best serve the Congress, and to provide guidance on what legislative developments are occurring and what the Congress's priorities are. We are very grateful for that support and guidance, which are key to our success.

Since I last testified about CBO's work before you in May 2015, the agency has continued to work diligently to carry out its mission and has emphasized five areas of work that are of particular interest to the Committee:<sup>1</sup>

First, to respond to the needs of the budget committees, CBO has prepared a multitude of cost estimates, both formal and informal, to support the committees' role in budget enforcement, as well as in the development of a budget resolution.

Second, CBO continues to press to make its analysis transparent. Its publications go well beyond simply presenting results; instead, the agency works hard to explain the basis of its findings so that Members of Congress, their staff, and outside analysts can understand the results and the methodologies used. For example, the agency has supplemented reports about the budgetary effects of health insurance subsidies and hurricane damage with working papers detailing, respectively, its approach to estimating the effects of the Affordable Care Act on the labor market and its approach to estimating expected hurricane damage.<sup>2</sup>

Third, CBO has emphasized "dynamic analysis." For example, in response to the requirement for certain dynamic analyses specified in concurrent budget resolution for fiscal year 2016, CBO (in collaboration with the staff

of the Joint Committee on Taxation) completed several such estimates for H.R. 3762, the Restoring Americans' Healthcare Freedom Reconciliation Act. The agency also solicited extensive feedback on its methods as it continues to refine and enhance its modeling approaches.

Fourth, CBO has devoted significant resources to analyzing trade agreements and improving its capability to model their effects. The agency continues to prepare to analyze potential legislation related to the Trans-Pacific Partnership.

Finally, CBO continues to devote resources to attracting and retaining talented people and developing their skills. Among the notable staffing changes, Mark Hadley became the agency's Deputy Director in June, and two new Assistant Directors—one for macroeconomic analysis and the other for tax analysis—joined the agency this year.

In the coming year, CBO will:

- Continue to be guided by its mission and core values;
- Aim to expand its analytical capacity—with an emphasis on macroeconomic analysis, health care issues, and modeling capabilities; and
- Focus on meeting three broad goals—continuing to provide the Congress with budget and economic information that is objective, insightful, and timely; presenting and explaining the methodology and results of CBO's analyses clearly; and improving CBO's internal management.

### CBO's Mission to Serve the Congress

The Congressional Budget Act of 1974 instituted a formal process through which the Congress could develop, coordinate, and enforce its own budgetary priorities. It also created legislative institutions to implement the new Congressional budget process: the House and Senate Budget Committees to oversee execution of the budget process and CBO to provide the budget committees and the Congress with objective, impartial information about budgetary and economic issues. CBO's work follows

1. See the testimony of Keith Hall, Director, Congressional Budget Office, before the Senate Committee on the Budget, *The Work of the Congressional Budget Office* (May 19, 2015), [www.cbo.gov/publication/50177](http://www.cbo.gov/publication/50177).

2. See Edward Harris and Shannon Mok, *How CBO Estimates the Effects of the Affordable Care Act on the Labor Market*, Working Paper 2015-09 (Congressional Budget Office, December 2015), [www.cbo.gov/publication/51065](http://www.cbo.gov/publication/51065); and Terry Dinan, *CBO's Approach to Estimating Expected Hurricane Damage*, Working Paper 2016-02 (Congressional Budget Office, June 2016), [www.cbo.gov/publication/51610](http://www.cbo.gov/publication/51610).

processes specified in that law and subsequent laws or developed by the agency in concert with the budget committees and the Congressional leadership. The agency's chief responsibility under that law is to help the budget committees with the matters under their jurisdiction. The agency also supports other Congressional committees—particularly the Appropriations, Ways and Means, and Finance Committees, as required by the Budget Act—and the Congressional leadership.

To fulfill its mission to serve the Congress, CBO does the following:

- Prepares reports on the outlook for the economy;
- Analyzes trends and recent developments related to federal spending and revenues and constructs budget projections for the next 10 years and the longer term;
- Estimates the effects of the President's budgetary proposals and numerous alternative policy choices on the budget and the economy;
- Estimates the cost of legislative proposals—which involves providing formal cost estimates for all bills reported by committees of the House and Senate, many more informal cost estimates while legislation is being developed, estimates of the cost of all appropriation bills, and estimates of the cost of a great many amendments as legislation is considered by the House and Senate;
- Estimates the cost of intergovernmental and private-sector mandates in reported bills;
- Conducts policy studies of governmental activities, policy choices facing lawmakers, and other developments that have significant budgetary and economic impacts; and
- Provides testimonies on a broad range of budgetary and economic issues.

In 2015, CBO produced more than 600 formal cost estimates and mandate statements, thousands of informal estimates, more than 100 "scorekeeping" tabulations for appropriation acts, and multiple budget projections and economic forecasts. In addition, the agency released more than 90 analytic reports and working papers.<sup>3</sup> In 2016, the pace of work is much the same.

To carry out its mission, CBO has requested an appropriation of \$47.6 million for fiscal year 2017, an increase of \$1.1 million, or 2.4 percent, from the \$46.5 million provided to the agency for 2016.

### CBO's Core Values and Related Policies

In a 1976 memorandum, CBO's founding director, Dr. Alice Rivlin, enunciated some of the agency's core values:

*As we begin the first full year with the new Congressional budget procedures in place, I want to emphasize once again that CBO must be, and must be perceived to be, an objective, non-partisan, professional organization in the service of the Congress. . . . Our work and our publications must always be balanced, thorough and free of any partisan tinge. . . . Our task is to provide information which will help the whole Congress in reaching its decisions.*

The agency is committed to providing information that is:

- Objective—representing not the personal opinions of CBO staff but the consensus and diversity of views of experts from around the country;
- Insightful—applying the best new evidence and innovative ideas as well as the lessons of experience;
- Timely—responding as quickly as possible to the needs of the Congress; and
- Clearly presented and explained—so that policymakers and analysts understand the basis for the agency's findings and have the opportunity to question the analysis and methods used.

In keeping with CBO's mandate to provide analysis that is objective and impartial, the agency makes no policy recommendations. Instead, it strives to present fully and fairly the likely consequences of alternative proposals being considered by the Congress so that lawmakers can make informed policy choices.

3. For more details, see Congressional Budget Office, *The Congressional Budget Office's Work in 2015: A Report to the Congress* (April 2016), [www.cbo.gov/publication/51290](http://www.cbo.gov/publication/51290). CBO will update that report on a regular basis.

In conducting its work, CBO reviews studies by others; reviews historical data for federal programs, as well as any data available from states for many key grant programs; and does original research using administrative records and survey data. CBO evaluates the evidence by considering how generalizable the research findings are to a proposed policy, what sorts of biases might affect the results of a study, what the middle of the distribution of possible outcomes might be, and how the uncertainty of the results can be characterized.

All of CBO's estimates and reports are reviewed internally for objectivity, analytical soundness, and clarity. That rigorous process involves multiple people at different levels in the organization. In addition, CBO consults with numerous outside experts who represent a variety of perspectives. The experts include professors, analysts at think tanks, representatives of industry groups, other experts in the private sector, and people working for federal agencies and for state and local governments. Whenever practical, CBO's analytic reports are reviewed by outside experts who specialize in the issue at hand and who have diverse views about the topic being analyzed and methods of analysis. In some cases, those experts are members of CBO's Panel of Economic Advisers or Panel of Health Advisers. Although such experts provide considerable assistance, CBO is solely responsible for its work.

Maintaining high-quality work in the face of its many demands is something CBO takes very seriously. The agency must balance its commitment to respond quickly to the Congress's needs with its professional responsibility to release reports and estimates only when they reach sufficient quality. Part of CBO's success is built upon its ability to strike that balance. Still, at times, CBO's analyses may take longer than the Congress hopes.

CBO is also committed to maintaining a level playing field with regard to the information and analysis that it provides—ensuring that its work is made widely available to the Congress and the public. The agency releases publicly all of its formal cost estimates and analytic reports. It delivers its work to interested Members of Congress and their staff, including, in particular, the sponsor of legislation or requester of a report, the Chairman and Ranking Member of the committees of jurisdiction, and the budget committees. At about the same time, the agency posts the work on its website. In addition, an email service,

Twitter announcements, and RSS (really simple syndication) feeds notify subscribers when the agency publishes work. CBO continually strives to make its work more accessible on its website and on its social media platforms. For example, the agency has made a number of enhancements to the website, including creating a special collection for major recurring reports; displaying in one place the spreadsheets that show baseline budget and economic projections prepared in various years; displaying in another a collection of the detailed baseline projections for selected major programs; and making information about the budgetary effects of policy options in separate reports searchable by topic online.<sup>4</sup>

In some circumstances, though, the needs of the Congress lead CBO to keep the results of an analysis confidential. Such analyses include informal cost estimates and other types of information produced to assist in the development of legislation. Those informal communications do not undergo the same review required for formal estimates. They are often prepared when committees are evaluating alternative proposals to accomplish their goals, have not made any specific proposals public, and need the flexibility to modify their proposals before they become public, sometimes in response to CBO's preliminary estimates. In fact, CBO's analysts often provide informal, preliminary estimates to committee staff for a broad range of legislative options, making possible the consideration of different approaches before a specific legislative path is decided upon. In such situations, CBO recognizes that the confidentiality of its work is critical to committees' deliberations, so it keeps its informal estimates confidential as long as the proposals are not made public. (Such confidentiality generally does not apply to proposals that differ only in minor details from ones that are in the public domain.) However, once such a proposal becomes public—as introduced legislation or through public discussion of its major elements—CBO makes its estimate for that proposal available to any interested party in the Congress.

4. See Congressional Budget Office, "Major Recurring Reports," [www.cbo.gov/about/products/RecurringReports](http://www.cbo.gov/about/products/RecurringReports), "Budget and Economic Data," [www.cbo.gov/about/products/budget\\_economic\\_data](http://www.cbo.gov/about/products/budget_economic_data), "Baseline Projections for Selected Programs," [www.cbo.gov/about/products/baseline-projections-selected-programs](http://www.cbo.gov/about/products/baseline-projections-selected-programs), and "Budget Options," [www.cbo.gov/budget-options](http://www.cbo.gov/budget-options).

### CBO's Efforts to Expand Its Analytical Capacity

CBO continually strives to improve its analytical capacity. Currently, the agency is giving special emphasis to three areas:

- Analyzing the economic effects of federal tax and spending policies, including conducting “dynamic analysis” of certain legislation,
- Analyzing health care issues, and
- Expanding modeling capabilities and access to data.

To support the first two items above, CBO seeks to boost its staffing by three new full-time-equivalent positions (FTEs)—from the 235 FTEs supported by the 2016 appropriation to 238 for 2017. About one-third of the requested increase in CBO's budget, \$391,000, would fund those new positions.

#### Dynamic Analysis

In May 2015, the Congress adopted a concurrent resolution on the budget for fiscal year 2016 requiring CBO, to the greatest extent practicable, to incorporate macroeconomic effects into its cost estimates for major legislation approved by Congressional committees. In response, CBO (in collaboration with the staff of the Joint Committee on Taxation) completed several such estimates in the past year. Because macroeconomic analyses require complex modeling and a significant amount of time, they can be produced for only a small number of major proposals, and only if time allows.

CBO has devoted significant effort to developing and enhancing analytical tools that enable the agency to assess the macroeconomic effects of fiscal policies. In selected reports—as distinguished from cost estimates—CBO has provided estimates of the effects that significant changes in federal spending and tax policies would have on the overall economy. Some of those analyses have also examined how the projected changes in the economy would in turn affect the federal budget. Since May 2015, the agency has incorporated dynamic analysis in its annual report on the long-term budget outlook; once again in its annual examination of the economic impact of the President's budget and in reports about alternative budgetary paths; and in reports on the macroeconomic effects of federal investment, of repealing the Affordable Care Act, and of eliminating automatic reductions to discretionary

spending caps. Notably, in *The 2016 Long-Term Budget Outlook*, all of CBO's projections beyond 2026 incorporate, for the first time, the macroeconomic effects of fiscal policy under current law.<sup>5</sup>

CBO expects to devote considerable attention to further developing its capacity to conduct dynamic analysis in the coming year, so that it can effectively carry out the requirements specified in the budget resolution. Cost estimates that incorporate dynamic analysis will include all of the information typically presented in cost estimates as well as information on the macroeconomic effects and the uncertainty surrounding those effects. To the extent possible within the time available, CBO will explain the basis for determining the budgetary impact of macroeconomic effects. The agency has already shifted some resources to bolster its dynamic analysis and has requested funding for additional staff to work on such analyses.

#### Analysis of Federal Health Care Spending

CBO faces significant challenges in projecting the future costs of federal health care programs and in analyzing proposals to change those programs. Although spending for health care in the United States has grown more slowly in recent years than it had previously, health care spending per person has grown faster, on average, than the nation's economic output per person during the past few decades.

CBO expects that federal spending on the government's major health care programs will continue to rise substantially relative to the size of the economy, though the estimates are subject to a considerable degree of uncertainty. A particular challenge is assessing the extent to which the recent slowdown in the growth of health care spending results from temporary factors like the recession or, instead, reflects more enduring developments. CBO has found no direct link between the recession and slower growth in spending for Medicare. Accordingly, over the past several years, CBO has substantially reduced its 10-year and long-term projections of spending per person for Medicare, for Medicaid, and for the country as a whole. However, the growth rates for such spending per person are expected to rebound somewhat from their recent very low levels.

5. See Congressional Budget Office, *The 2016 Long-Term Budget Outlook* (July 2016), [www.cbo.gov/publication/51580](http://www.cbo.gov/publication/51580).



Interest in legislative proposals related to health care—on the part of committees of jurisdiction, the Congressional leadership, and the budget committees—remains very high. The enactment of the Affordable Care Act in 2010 has been followed by a great deal of Congressional interest in analysis of that legislation and of possible modifications to it, as well as potential changes to Medicare and Medicaid. Several developments could boost that interest, along with CBO's workload. For instance, more data will become available about the costs of the expanded health insurance coverage under the Affordable Care Act, which will further understanding of potential effects of changing that law.

CBO is in the process of analyzing various aspects of the health care system and enhancing its analytical capacity to assess the effects of future legislation on that system and on the federal budget. In particular, it is incorporating new data from the Current Population Survey into its simulation model of health insurance coverage and reviewing and updating every aspect of that model, which forms the backbone of its budget projections and cost estimates related to federal health care spending for people under age 65.

#### **CBO's Modeling Capabilities and Access to Data**

In addition to enhancing its capability for dynamic analysis and its capacity to assess the effects of future legislative proposals on the health care system and on the federal budget, CBO is also working to expand its capacity to analyze energy and environmental issues. Furthermore, CBO expects to expend considerable effort to enhance its access to data (such as earnings data reported by employers to government agencies matched with survey data and health insurance claims records) to improve the analyses the agency produces.

*Expand the Capacity to Assess Energy and Environmental Proposals.* CBO is expanding its capacity to assess the effects of future legislation on energy markets and the environment. In particular, the agency has procured the licenses necessary to make use of the Energy Information Administration's National Energy Modeling System (NEMS) to both expand the scope of policy proposals that CBO can examine in detail and to improve the consistency of the analysis across proposals.

The use of NEMS will increase CBO's ability to estimate the effects of changes to energy policy on the prices and production of different types of fuels and on the economy

as a whole, among other outcomes. For instance, expanding its capacity in that way will allow CBO to:

- Assess policy changes that would allow oil and gas production on more federally controlled lands (both onshore and offshore);
- Evaluate the effect of potential changes in Corporate Average Fuel Economy, or CAFE, standards; and
- Model the effects of potential changes in the requirements for the use of renewable fuels in transportation or electricity generation.

*Enhance and Expand CBO's Access to Data.* In the coming year, CBO would like to hold more data at the agency, both data that analysts now use regularly and new data that the agency hopes to obtain. The resulting access (both speedier and more consistent) would benefit CBO's work—its budget projections for the next 10 years and the long term, cost estimates for legislative proposals, and policy studies of issues that have significant budgetary and economic impacts—as well as the timeliness of the work.

For example, enhanced and expanded access to data would allow CBO to:

- Enhance its projections of educational attainment, thereby improving its projections of total factor productivity and economic growth;
- Improve its modeling of various demographic characteristics—including marriage patterns and the variation in fertility and mortality rates by socioeconomic status—which would bolster projections of Social Security benefits and income tax receipts;
- Improve its understanding of payment rates for health care goods and services in commercial insurance plans and in privately run Medicare Advantage plans and of the factors affecting those rates, thereby enhancing the agency's ability to model proposals affecting private insurance or establishing a "premium support" system for Medicare;
- Better its understanding of the resources available to people in retirement, which would allow the agency to expand its recent analysis of families' wealth to also consider Social Security income and income from defined benefit pensions;

- Enhance its understanding of labor force participation at older ages and changes in earnings inequality over time, which would improve projections of Social Security benefits and people's behavior in claiming benefits; and
  - Better its understanding of the costs of operating military forces, which would improve projections of defense spending.
- CBO is grateful for the help the budget committees have given when the agency has sought data in the past and hopes to continue working together on future efforts.

### Three Broad Goals for CBO

On a broader scale, in carrying out its mission of serving the Congress during 2016 and 2017, CBO will focus on meeting three goals:

- Continue to provide the Congress with budget and economic information that is objective, insightful, and timely.
- Continue to present and explain the methodology and results of CBO's analyses clearly.
- Continue to improve CBO's internal management.

### Continue to Provide the Congress With Budget and Economic Information That Is Objective, Insightful, and Timely

By the end of this year, CBO expects that it will have provided the following estimates and other analyses to the Congress (in quantities roughly similar to last year's):

- About 20 reports presenting assessments of budgetary developments during the current fiscal year, the outlook for the budget and the economy, analyses of the President's budget, long-term budget projections, and options for reducing budget deficits;
- More than 600 formal cost estimates, all of which will include not only estimates of federal costs but also assessments of the cost of mandates imposed on state, local, and tribal governments and on the private sector;

- Thousands of preliminary, informal cost estimates, the demand for which is very high as committees seek to have a clear picture of the budgetary impact of proposals and variants of proposals before they formally consider legislation;
- More than 100 scorekeeping tabulations, including account-level detail for individual appropriation acts at all stages of the legislative process and summary tables showing the status of discretionary appropriations (by appropriations subcommittee) and running totals on a year-to-date basis; and
- Roughly 75 analytic reports and other publications—generally required by law or prepared in response to requests from the Chairmen and Ranking Members of key committees—on a broad range of topics, including health care, Social Security, policies for increasing economic growth and opportunity, changes in benefit programs, defense policy, infrastructure, energy policy, and the government's role in the financial system. Those publications explain developments, provide information about the effects of alternative policies, explain current and alternative budgetary concepts used to estimate costs, and enhance CBO's transparency about its models and procedures; in doing those things, the projects convey important information to the Congress and improve the agency's capabilities for future analyses.

Such a body of analysis requires very hard work by CBO's highly dedicated staff. Nevertheless, the agency expects that the anticipated volume of estimates and other analyses it can produce will fall considerably short of the number of Congressional requests, especially with regard to health care issues. In addition to the interest in analyses of the Affordable Care Act and possible modifications to it, committees are considering many other types of proposals for changes in federal health care programs. Also, the slow recovery from the economic downturn has spurred interest in the agency's economic forecasts and in policies that might affect economic growth and opportunity in both the near term and the longer term. Other time-sensitive issues arise frequently and add to an already heavy workload: Over the past year, for example, CBO analyzed legislation related to the privatization of the air traffic control system, Puerto Rico's debt crisis, sentencing reform, trade facilitation and the enforcement of certain trade laws, child nutrition programs, and child welfare programs.

Analyzing proposals has strained the agency's resources in many areas. As a result, responding in a balanced way to requests from both the majority and minority of multiple committees in both the Senate and the House is a continuing challenge. CBO regularly consults with committees and the Congressional leadership to ensure that its resources are focused on the work that is of highest priority to the Congress.

#### **Continue to Present and Explain the Methodology and Results of Analyses Clearly**

CBO works hard to make its analysis transparent. To begin with, CBO's publications go well beyond simply presenting results; instead, the agency explains the basis of its findings so that Members of Congress, their staff, and outside analysts can understand the results and the methodologies used. In particular, although much of the work that CBO does is extremely technical in nature, the agency devotes substantial time and energy to presenting the work as clearly and nontechnically as possible. It continually seeks feedback about those efforts in order to ensure their effectiveness.

CBO also seeks extensive external review of the agency's analytic reports before they are released and of the methodologies on which its products are based.

In the coming year, input from outside experts and extensive external review will remain an important component of transparency:

- CBO will continue to solicit external professional review of its work so that the agency's analyses reflect both the consensus and diversity of views of a range of experts from around the country.
- The agency's cost estimates will draw on consultation with outside experts.
- The agency's Panel of Economic Advisers will meet twice to provide input on the agency's latest economic forecast and other issues, and the agency's Panel of Health Advisers will meet to discuss key issues affecting the agency's baseline projections and analyses of proposals and to examine new research in health care and health care financing. CBO will also regularly consult with those distinguished experts and other experts for guidance on the agency's work on a broad range of topics.

CBO also aims to clearly present the evidence underlying its analyses and how the agency assesses that evidence. To that end, CBO's documents and related information will aim to go well beyond presentations of results:

- Formal cost estimates will describe the basis for the estimate—that is, the information that CBO collected and how that information was used in constructing the estimates.
- The agency will document and explain the revisions to its budget projections in each successive baseline, and it will report on the accuracy of its projections. CBO released an assessment of the accuracy of its revenue projections in November 2015 and within the next year will do so for its spending projections and its economic forecasts.<sup>6</sup>
- The agency will publish supplemental data and other technical information with its key reports.
- Many of CBO's reports will provide substantial discussions of the relevant research literature and CBO's modeling approaches—in the text, in separate boxes, or in appendixes.
- CBO will increase public documentation of its most significant modeling efforts—by publishing background reports and working papers providing details about its analyses for nonexperts and technical descriptions for experts. In particular, the agency will publish working papers explaining its updated and enhanced model of the health insurance system and the models used in CBO's macroeconomic analysis.

And the agency will promote transparency by providing broad access:

- When CBO completes a budget or economic projection, a cost estimate for a public piece of legislation, or another type of analysis, it will make the results of that analysis available immediately to all Members of Congress, their staff, and the public.
- CBO's analysts will regularly explain details underlying the agency's estimates and other analyses to interested Congressional staff.

6. See Congressional Budget Office, *CBO's Revenue Forecasting Record* (November 2015), [www.cbo.gov/publication/50831](http://www.cbo.gov/publication/50831).

- CBO will regularly update pages on its website about dynamic analysis and methods for analyzing health insurance coverage to make its work in those areas easier to find.
- To promote discussion among experts in the field, CBO's analysts will present their work—including descriptions of their modeling approaches—in working papers and at professional conferences.
- CBO will enhance portions of its website to help Congressional staff better understand how to work with CBO.

Examples from CBO's past work illustrate other aspects of the agency's commitment to transparency. For instance, when CBO revised its views of the effectiveness of malpractice reform in reducing health care costs, of the effect of prescription drug use on Medicare's spending for other health care services, and of the effect on the budget deficit of raising Medicare's age of eligibility to 67, it issued reports explaining why. In recent reports, CBO explained how it assesses the budgetary effects of the United States' participation in the International Monetary Fund and why it projects that actual output will be below potential output, on average.<sup>7</sup> Analyses of security issues have included supplemental information about how CBO models cost growth in the construction of new ships and other new weapon systems, and the costs of detecting dangerous cargo in shipping containers.<sup>8</sup>

In addition, CBO undertakes and publishes analyses of the sensitivity of its estimates to key parameters. For example, CBO's analyses of the economic effects of fiscal policies include alternative estimates that would apply if various effects were stronger or weaker than expected—such as the amount of short-term restraint provided by higher taxes or lower government spending or the

response of the labor supply to changes in tax rates. Similarly, an analysis of employment-based health insurance under the Affordable Care Act showed how the results would vary if employers' and employees' responses to that act differed from the agency's expectations.

The agency often responds to questions from Members of Congress about the methods used in its analyses. CBO's analysts spend a great deal of time meeting with interested Members of Congress and their staff to explain the details underlying cost estimates and reports. In its blog, CBO also highlights answers to questions from Members, sometimes explaining what the limitations of its analyses are and how new data and results from well-designed studies could help the agency better predict the potential effects of legislative proposals.

Even though CBO devotes substantial time and energy to presenting its work as clearly and nontechnically as possible, the pace of Congressional action often requires the agency to produce analyses quickly. So the amount of explanation that can be provided when an estimate or analytic report is released is sometimes limited by the time available. And because the overall demand for CBO's work is high and its resources are constrained, the agency needs to balance requests to explain more about finished analyses with requests for new analyses and with its other responsibilities, such as regularly updating its baseline budget and economic projections.

#### Continue to Improve Internal Management

In addition to focusing directly on serving the Congress, CBO devotes resources to attracting and retaining talented people, developing their skills, and providing the support services and other infrastructure needed to make them as productive as possible.

Nevertheless, CBO continues to face considerable competitive pressure in attracting and retaining the highly educated and skilled employees that it needs. More than two-thirds of CBO's staff consists of economists and budget analysts. Talented people with those backgrounds are highly sought by other government agencies, private analytic organizations, universities, and private companies. Some of CBO's economists and budget analysts could earn significantly higher compensation working in the private sector or other government agencies in both the executive and legislative branches. For example, both the Office of Management and Budget and the Government Accountability Office have the authority to pay significantly more

7. See Congressional Budget Office, *The Budgetary Effects of the United States' Participation in the International Monetary Fund* (June 2016), [www.cbo.gov/publication/51663](http://www.cbo.gov/publication/51663), and *Why CBO Projects That Actual Output Will Be Below Potential Output on Average* (February 2015), [www.cbo.gov/publication/49890](http://www.cbo.gov/publication/49890).

8. See Congressional Budget Office, *An Analysis of the Navy's Fiscal Year 2016 Shipbuilding Plan* (October 2015), [www.cbo.gov/publication/50926](http://www.cbo.gov/publication/50926), *Long-Term Implications of the 2016 Future Years Defense Program* (January 2016), [www.cbo.gov/publication/51050](http://www.cbo.gov/publication/51050), and *Scanning and Imaging Shipping Containers Overseas: Costs and Alternatives* (June 2016), [www.cbo.gov/publication/51478](http://www.cbo.gov/publication/51478).

than CBO does. In addition, most of CBO's staff who are not economists or budget analysts work in fields with competitive private labor markets; that group includes information technology professionals, lawyers, and others.

To attract and retain talented employees, CBO relies heavily on the nonmonetary rewards of working at the agency. Fortunately, the appeal of the agency's mission to provide objective analyses, the intellectual challenges, the open and collaborative culture that the agency has maintained since its founding, and the satisfaction of public service have enabled CBO to build a dedicated and skilled workforce. However, with the current limits on the salaries that CBO can pay in the competitive markets for economists, budget analysts, and other professionals, hiring and retaining strong performers will be difficult over the long term.

Since I last testified before the committee about the work of CBO on May 19, 2015, there have been several significant staffing changes.

Most notably, on June 6, 2016, **Mark Hadley** became CBO's Deputy Director. He has served CBO for 15 years in a variety of capacities. He started his CBO career as an analyst in the Budget Analysis Division, where he worked on cost estimates and projections related to deposit insurance, aviation, and commerce. After earning his law degree, he spent a few years in the private sector and then returned to CBO in 2006 as Deputy General Counsel. In 2008, he became General Counsel and served in that position until becoming the Deputy Director. Mr. Hadley has a J.D. degree from The George Washington University Law School and a master's degree in public affairs from the Robert M. La Follette School of Public Affairs at the University of Wisconsin. He received his B.A. from Truman State University.

In August 2016, **John McClelland** became Assistant Director for Tax Analysis following 18 years at the Department of the Treasury. At that agency, he most recently was Special Assistant to the Director of the Office of Tax Analysis (OTA). Before that, at OTA, he was the Director of Revenue Estimating; in that role, he was responsible for the Administration's estimates of the revenue consequences of all tax proposals. Over the course of his tenure at OTA, he worked on a variety of topics in taxation, with a particular focus on business taxes and the consequences of potential reforms. Earlier in his time at the Treasury Department, he was the ana-

lyst responsible for the forecasts of revenues from the corporate income tax and a variety of excise taxes. He received his doctorate in economics from the University of Maryland, College Park. He received his bachelor's degree in economics, mathematics, and environmental studies from Bowdoin College.

In January 2016, **Wendy Edelberg** became an Associate Director for Economic Analysis, having served as the Assistant Director for Macroeconomic Analysis for almost five years. Just before coming to CBO in 2011, she was the executive director of the Financial Crisis Inquiry Commission, which released its report on the causes of the financial crisis in January 2011. Previously, she worked on issues related to macroeconomics, housing, and consumer spending at the President's Council of Economic Advisers during two administrations. Before that, she worked on those same issues at the Federal Reserve Board. She received a Ph.D. in economics and an M.B.A. from the University of Chicago, and a B.A. from Columbia University.

**Jeffrey Werling** joined CBO in January 2016 as Assistant Director for Macroeconomic Analysis. Before coming to the agency, he was the Director of Inforum, a research unit within the Department of Economics at the University of Maryland, College Park. There, he served as the principal investigator for projects concerning economic forecasts, infrastructure investment, health care, fiscal policy, port disruptions, immigration, and exchange rate fluctuations. For more than a decade, he contributed to the *Blue Chip* and other consensus economic forecasts. Previously, he held positions as an international and industry economist with the National Electrical Manufacturers Association, the Manufacturers Alliance for Productivity and Innovation, and Wharton Econometric Forecasting Associates (now Global Insight). He received an M.A. and a Ph.D. in economics from the University of Maryland and a B.S. in mineral economics from the Pennsylvania State University.

**Leigh Angres** became CBO's Associate Director for Legislative Affairs in July 2015. She joined CBO in 2007 and has served in a variety of capacities since then. Most recently, she was the special assistant to the Director for five years, during which time she was responsible for preparing the Director's presentations, managing CBO's blog, and writing reports about deficit reduction. Before joining the Director's office, she was an analyst in the Budget Analysis Division. In earlier government service, she was a budget analyst in the Department of Justice's

Civil Division, preparing the agency's appropriation requests. She received her M.P.P. from the University of California at Berkeley and her A.B. from Duke University.

In addition to those arrivals and promotions, other important staffing changes have occurred. In the Budget Analysis Division:

- Sheila Dacey became Chief of the Income Security and Education Cost Estimates Unit and
- Adam Wilson became Chief of the Scorekeeping.

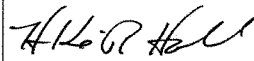
Elsewhere in the agency, the following management changes happened in 2016:

- Linda Bilheimer, who led the Health, Retirement, and Long-Term Analysis Division, became a senior adviser in that division;
- Kim Kowalewski, who served as Deputy Assistant Director in the Macroeconomic Analysis Division, became a senior adviser in that division;

- Alexandra Minicozzi became a senior adviser in the Health, Retirement, and Long-Term Analysis Division;
- Felix Reichling became Chief of the Fiscal Studies Unit in the Macroeconomic Analysis Division; and
- Robert Sunshine, who served as CBO's Deputy Director for almost nine years, became a senior adviser in the Director's Office.

This testimony incorporates information from *CBO's Appropriation Request for Fiscal Year 2017*, which was testimony before the Subcommittee on the Legislative Branch of the Senate Committee on Appropriations presented on March 8, 2016.

This testimony is available on CBO's website, at [www.cbo.gov/publication/51923](http://www.cbo.gov/publication/51923).



Keith Hall  
Director



Chairman ENZI. Thank you for your testimony.

I will yield to Senator Johnson, then Senator King, then Senator Perdue before I ask my questions.

Senator JOHNSON. Thank you, Mr. Chairman. Welcome, Dr. Hall. Mr. HALL. Thank you.

Senator JOHNSON. You mentioned doing more and more work in terms of health care. It just so happens in my Committee, the Homeland Security Committee, tomorrow we are going to be holding a hearing on the current state of affairs in terms of the exchanges.

One of my concerns when I first came to the Senate and was on the Budget Committee, looking at what information we had in terms of potential cost implications of the Patient Protection and Affordable Care Act, it just never seemed like there was a specific line item, that tracking the ongoing costs of that act was going to be extremely difficult. Can you tell me with a little more specificity where CBO is at in terms of accumulating on an annual basis, you know, exactly what are you publishing, the exact costs of the health care law?

Mr. HALL. Well, sure. One of the things that we have done—and this is to your point about separating out the effects of the Affordable Care Act from other things—is we will be producing every spring the cost of health care and the subsidies for health care that will include the ACA as part of that. And we are going to continue to try to detail that as much as possible. And we really are anticipating getting some real data as we go forward and being able to use that data to talk about things, and this is going to be an important part to us of transparency. And a key for us, too, is adapting what we are doing to the realities of actually what happens in exchanges and elsewhere with health care.

Senator JOHNSON. So I tasked my staff this morning with giving me the current figures. Historically, since the ACA has been implemented, do you have that information? Again, I wish I knew whether we actually had it at our disposal or not. In other words, are they going to be able to give me a figure when I leave this hearing room?

Mr. HALL. Well, yes. I can tell you that right now we—just this March, we got some new data, and we have adapted our estimate of the number of people receiving health care through exchanges. We now think there are about 11 million people receiving health care through exchanges, and about 9 million of those are subsidized. That is actually a downward revision of about a million people from our previous estimate earlier this year.

And then we have got a new estimate of the subsidies. We now think there are about \$43 billion worth of subsidies this year, and that is going to be up about \$5 billion from last year. So those are the latest numbers based on data.

Senator JOHNSON. So last year, we had about \$38 billion in—how does that track with what the original estimate was for the health care law?

Mr. HALL. Well, I think our original estimate was a little high, a bit high. That was in large part, I think, because there was such an increase in getting medical help through Medicaid at the State level, that that sort of—that was much higher than we thought,

and the exchanges was a bit lower than we thought. And then, of course, our estimate of the average price of premiums was a bit high early on, and we have adapted that, where we still expect that price to go up over time.

Senator JOHNSON. The number of people expected to receive subsidies was initially forecast to be far higher than what we are looking at here, correct?

Mr. HALL. That is correct.

Senator JOHNSON. So on a subsidy per person—again, I do not have the figures. I would think the subsidy per person is higher than was originally estimated. Is that true or—

Mr. HALL. You mean the spending per person?

Senator JOHNSON. Yeah.

Mr. HALL. I would have to follow up on that. That sounds like that is right, the logic. But I do not know for sure.

Senator JOHNSON. Do you know exactly how much lower the subsidies, that \$43 billion, is versus the original forecast?

Mr. HALL. Not offhand. I will have to follow up. I am sorry. I do not know that.

Senator JOHNSON. Okay. I will be asking my staff that, so maybe—but you believe you have—CBO publishes that information, I will be able to get that for the hearing tomorrow?

Mr. HALL. Oh, yes. Yes.

Senator JOHNSON. Okay. I really have no further questions. Thank you.

Chairman ENZI. Senator King.

Senator KING. Thank you, Mr. Chairman. Dr. Hall, thank you for your good work.

I note that the budget of the Congressional Budget Office has essentially been frozen since 2010, even adjusting for inflation. Are you adequately funded to perform the functions that you are being asked to do?

Mr. HALL. Well, we have asked for a little bump up because we need it, in large part because—

Senator KING. You asked for \$1.7 million additional this year, I think?

Mr. HALL. Yeah. Yeah, it was—yeah, it was a few million. It was not very—we are looking to add at least basically three positions to help with the macro modeling in the health care work. We will still function fine without the money, but it really would help our move towards transparency and some other things.

Senator KING. Good. Dynamic scoring, very interesting economic theory. When you attempt to score something on a projected basis based upon effects on the macro economy, do expenditures get the same kind of dynamic scoring—in other words, an investment in education, which is expected to return higher taxes in the end by the people earning more money? Are expenditures dynamically scored as well as tax provisions?

Mr. HALL. We do try to do that. That is correct. To be honest, it is somewhat harder to do that, and we have been doing a bit more research so we can get better at that aspect of it. But that certainly is part of our plans, to be able to do that sort of work.

Senator KING. So it works both ways, in other words?



It is not just here is the positive effect of a tax cut. It is also here is a positive effect of an investment in education or highways or bridges or whatever infrastructure.

Mr. HALL. That is right. In fact, just this spring, maybe this summer, we produced a report on Federal investment, and what we have done is we have looked at the research and summarized what we think is the likely impact of Federal investment. We find that the research is pretty thin, unfortunately. But we have got a summary of that, and we are, in fact, doing some work to try to advance that.

Senator KING. Well, that was going to be my next question. The concept of dynamic scoring has been around for quite some time, and a lot of discussion.

Mr. HALL. Right.

Senator KING. Is there sort of actual versus projected studies that show whether the dynamic scoring works, whether it is accurate? The Chairman mentioned—he has called it “more accurate budgeting.”

Mr. HALL. Right.

Senator KING. But I wondered if there was any data to underlie that assertion.

Mr. HALL. There is a little bit on the Federal investment side, like I said, but that one is a bit thin.

One of the troubles on the spending side is the amount of time it takes for things to affect the budget. For example, if you look at education, well, that is not something—

Senator KING. Maybe a 30-year—

Mr. HALL. Exactly. That is one of the challenges.

Senator KING. I would argue, for example, that the GI bill is one of the most cost-effective programs in history, but the results did not come in for some years.

Mr. HALL. Right. And we have looked at the idea of trying to get a better handle on that, not so much in our scoring, because that is a different time frame, but in terms of research.

Senator KING. How about on the tax side? Are there any studies about the effect—the accuracy of dynamic scoring of tax changes?

Mr. HALL. Well, it is not specifically in dynamic scoring, but there is a bit more literature on the effect of taxes on economic growth. In fact, that is part of why we are more comfortable, I think, on the tax side in terms of our estimates. And that is guided, that is very much guided, our actual estimates, is what the literature actually says about this. But, again, just like anything else, we will have to keep looking at the literature and seeing if we are being correct in things.

It is really hard to specifically estimate the effects of dynamic scoring, specifically on what we do, because the changes often are not that big to sort of find an impact on GDP.

Senator KING. Now, when you are doing this scoring, are we presented with two sets of figures—one is here is the actual loss to the Treasury, and here is the analysis based upon a dynamic assumption of economic growth? Do we get both numbers now?

Mr. HALL. You do. We made the decision that every time we did a cost estimate that had dynamic elements to it, we would give you both numbers. So we would give you the estimate without the dy-

namic and the macroeconomic effects, and we would give you the estimate with the macro effects so you can actually see the different parts of that.

Senator KING. And it seems to me over a course of time we will have some data built up to see whether the projections under the dynamic scoring model are accurate.

Mr. HALL. I think that might be right. I think that is correct. We certainly look at how accurate our revenue estimates are and our spending estimates are on the Federal budget as a whole, and we have a plan to continue to look at how well we are doing there.

Senator KING. One of the problems with the whole concept is that it is not a single-factor analysis. In other words, the economy, as you know, is so complicated.

Mr. HALL. Yes.

Senator KING. We could have a dynamic score of a tax cut and say we should produce X, but then there is a housing crash or a terrorist attack that affects the economy, the economy does not grow, and it is impossible to point and say this did this and this did that. How do you account for that kind of uncertainty?

Mr. HALL. Well, it is hard to, and it is hard to in any kind of forecasting. If we just forecast the macro economy, we have exactly that issue. By putting the dynamic element into our cost estimates, I think it makes it more accurate, I believe it makes it more accurate; otherwise, we would not do it. But it does probably introduce some more uncertainty in our estimate than is already under our regular—

Senator KING. My only concern as a policymaker is that we not be seduced by the rosy projections that never manifest themselves.

My time is up, but for the record, I would really appreciate it if you could supply some studies of the dynamic effect of tax policy. You know, do tax cuts increase economic growth? That is what I am interested in seeing.

Mr. HALL. Sure, and I believe we do have some significant research papers on that.

Senator KING. That would be helpful. Thank you very much. Thank you, Doctor.

Chairman ENZI. Excellent questions. If you have some more, I can give you a little more time. We are not that—okay.

Senator KING. We have plumbed the shallows of my knowledge. [Laughter.]

Chairman ENZI. I know that that is not true. And in regard to one of the comments that you made, I know that forecasting is a lot easier if it was not about the future.

Last year, in your testimony you mentioned several goals that you had. One of them was, "The transparency of our work is very important and enhancing it is one of my prime objectives." What actions have you taken since you made that statement to increase the transparency? And how does that compare to efforts of the agency in previous years? I know you remain committed to increasing transparency. Do you have any new targets that you are working on that we ought to be aware of?

Mr. HALL. Sure, well, I have actually got a number of things I would like to mention. First of all, throughout our entire range of publications, we had an increased effort to be more transparent

and be more open about the basis for our analysis and the methodology used. Part of that has been some serious training and establishing some best practices, especially on cost estimates for our budget analysts to use and sort of describing more clearly how they arrived at their estimates. And, of course, here the basic goal is that we want to open ourselves up to feedback on how we are doing things.

The second thing is we produce a number of supplemental reports which are follow-ups intended to provide transparency. One example was last year we did produce an estimate of the removal of the Affordable Care Act with the macroeconomic effects included. We followed that up with a research paper describing the labor market effects of the Affordable Care Act, and that was the primary macro effects in that result. And so in that we detail exactly how we got to that number on the labor market, and hopefully we will get some feedback on that.

And something similar, I guess, on the—we also looked at the effect of potential increase in hurricane damage, and we also have—not only did we produce that likely effect over the next 30 years of increased hurricane damage, but we then produced a follow-up paper detailing the model exactly that we used so folks can imitate that.

In addition to our regular assessment of how our economic forecasting is doing, we compare ourselves to OMB and private sector forecasters just to see sort of how well we are doing. We have just done one on revenue projections, and we are working on one right now on spending projections. So we are going to have these regular reports to sort of tell you how we are doing in our forecasting. As you say, forecasting the future is difficult, but we are doing our best to sort of figure out how we are doing.

We have done a number of things with our website. We have got several spots—I would say at least four different spots on our website now where we are collecting things to increase transparency. For example, we have a home page on our website now that is dedicated to dynamic analysis. So on there, we are putting on all our research papers on dynamic analysis, and we will continue to populate that as we do more research and adapt our methods.

We have got a second page on health insurance, health care, so we are going to do the same. We have got some of our estimates, and we have got some presentations we have made to increase transparency. They are all there in one spot.

We also got a spot on the website that has spread sheets that show our baseline budget and economic projections historically. That makes it very easy for you to sort of see how we have forecasted things in the past as well as in the current.

And then we are providing a fourth spot that has a lot of detail on our baseline projections. You can see at a much more detailed level where our baseline projections are at any point in time, and we separated out some selected programs.

And then last, but not least, we are looking hard at one of our most important models where we are modeling health insurance coverage. That has been a real work horse for us. But the problem with that has been it is not very well documented. So what we

have done, we are now working on a second-generation model, and part of why we are doing this is we want to be able to incorporate actual data. It is not just the theoretical model. But as we are producing the model, we are going to be stopping and producing research papers and supplementary data to document the model as we go along over the next year.

So if you look at our output over the next year, you will see several papers coming out which, when the year is done, you will be able to stick them together, and we have got a documented model that people will be able to see, sort of see exactly how we are modeling the insurance markets.

Chairman ENZI. I am sure that will be helpful not only to us but to other people that are affected, too, so I appreciate your effort on that.

I know that many of the budget concepts that you use to estimate the costs of legislation and that the Budget Committee uses to enforce fiscal discipline, are decades old. It looks to me like most trace back to the President's Commission on Budget Concepts in 1967. How critical is it that the accounting rules and budgetary concepts be reviewed often and kept up to date? And is there anything we need to do to see that that happens?

Mr. HALL. Well, as you say, that document has been and continues to be very important for us. It is used a lot. It has some important recommendations. But it has been a long time, and there have been a significant number of issues that have arisen since 1967, and we have sort of dealt with that on a case-by-case basis. So I absolutely do think that something like a new budget concepts commission or some other format for reaching a consensus on a lot of these new issues that have popped up over the past almost 50 years I think would be very valuable to us and very helpful.

Chairman ENZI. Good suggestion. Thank you.

Now, over the last year, we have seen some errors in the CBO reports such as mistakes in the calculations of the Social Security replacement rates, in your long-term projections and cost estimates, also in the Water Resource Development Act in which the PAYGO score went from an estimated savings of \$6 million to a deficit of \$300 million once it was corrected. We just had that debate on the floor. To your credit, these errors have been publicly acknowledged and promptly corrected. However, it does raise the question about the review process.

Can you explain how decisions are made, particularly on whether you seek outside review? What is done to get the cost estimates correct? How do you find out that there has been mistakes?

Mr. HALL. Sure. Well, let me say I have been at a number of places in the Federal Government now, and CBO probably has the most extensive review process for analytical reports that I have seen. We have a great deal of internal review, and we are focusing on objectivity and analytical soundness and clarity in those things. But in analytical reports, in terms of external review, almost any time we have got enough time, we get external review. And it is targeted for outside experts with a wide variety of views on things, so we sort of get several things from that. We make sure that we are objective. We make sure that we are somewhat in the middle of the profession on topics. And hopefully folks help us catch errors,

if there are some errors in there, as we go along. That is an important thing. We will continue to do that.

Also, it so happens that the last few months we have, in fact, been looking at our review process on analytical reports and thinking about adapting that somewhat. And we are getting fairly close to enacting some of that, so we will do that, and I do think that we will probably make sure that we look at the issue of errors, not just, you know, the objectivity and soundness and clarity, but make sure that what we are doing is actually correct. But we are human, and that happens.

On cost estimates, that is actually a different process, and one of the issues for us with cost estimates is, frankly, you guys are often in a real hurry. And the most often phone call I get is questions about, "When will you be done?" So we actually always have this issue of we want to be thorough in a cost estimate, we want to be balanced and correct, and we want to be accurate, and sometimes you all are in a hurry. So we continue to worry about that balance on things.

Actually, in that area I think we have been remarkably accurate. With the 114th Congress so far, we have actually produced almost 1,400 formal cost estimates, and a very small handful have involved errors where we have had to submit a revision. In fact, we count only about four of those.

Nevertheless, we actually have been actively exploring ways to improve our review process. Part of it is for increased transparency. Part of it is because of the heavy workload for our managers. But part of it will be ways to sort of increase the accuracy of what we do.

Chairman ENZI. Thank you, and I have run quite a bit over. I still have more questions, but I appreciate Senator Whitehouse being here. I have enjoyed working with him on trying to get some budget reform that we still need to do, and so I will turn the time over to Senator Whitehouse.

Senator WHITEHOUSE. Thank you, Chairman. I concur that we still need to do that, and I look forward to continuing to work with you on that issue. I think it is very important, and working with you on it has been a pleasure. And for the record, let me say that I have just come in, so the Chairman, in going over his time, was not inconveniencing me or anybody else. He was having a discussion in a room in which nobody was champing at the bit for their turn. So I appreciate him yielding now so that I could ask a question or two.

First of all, welcome, Dr. Hall. Thank you.

Mr. HALL. Thank you.

Senator WHITEHOUSE. One of the recurring issues that we have to deal with on the Budget Committee is the cost of health care, particularly the projections into the outer years, which tend to dominate the conversation about our national debt.

We have seen since the Affordable Care Act the budget projections that CBO has put out for Medicare, Medicaid, and other health programs drop pretty substantially. For example, you guys look forward to the 2017 to 2026 period and identify it as a time horizon in which to make projections. And now you are projecting for that time period \$2.9 trillion less in health care spending than

CBO was projecting back just in 2010. So that is a very big move, a \$3 trillion move in a 10-year period over the 6 years that have taken place since then. It is about 60 percent of the \$5 trillion that we are projected to spend on Medicaid, so it is a big, big number. And I am interested in exploring with you ways in which we can try to get whatever policy signals we should be getting out of that change.

I am, as I think most people on this Committee know from my perennial remarks on this subject, kind of a maven of delivery system reform. I continue to remark on the inefficiency of our health care system compared to the OECD countries and the rather parlous life expectancies that Americans have with respect to their OECD neighbors.

You have said that CBO, and I will quote here, “has found no direct link between the recession and slower growth in spending for Medicare.” So if there is not a direct link with the recession, then presumably other things did have that effect. I am hoping that what had that effect is the increased focus on that quality and cost nexus that we are seeing out there in a great deal of the privacy that is driven or rewarded to a certain degree by the ACOs but that has its own momentum going, and there are groups like Intermountain and Geisinger and Gundersen Lutheran that are private sector leaders in all of that.

So if you could comment on that a little bit, I would be grateful to you.

Mr. HALL. Sure. In the past, and certainly we will in the future, we based our forecasting on historical rates, to a large degree, and certainly what has happened is in recent years health care spending has grown more slowly than historical rates would suggest, and we have adapted to that. We have lowered our estimates.

One of the things that is tricky for us, of course, is we did just come out of the Great Recession, so it is hard to separate temporary versus more permanent effects from that. And I think that is going to be one of the things that we are going to continue to try to focus on to try to get that right and make sure that we identify some sort of permanent slowdown that is there.

Senator WHITEHOUSE. So can you kind of back up a step and, rather than comment on the phenomenon itself, comment briefly on what you think the most prudent steps would be for CBO to undertake to try to tease out of all that information what seems to be working and what does not seem to be working? Are there things you could look at that would provide a model that would allow you to back out some of the projection savings or otherwise adjust for this? And what are you doing to achieve that?

Mr. HALL. Well, certainly one of the things that we are doing—I mentioned a little bit a minute ago when we were looking at a large model for health insurance that we are doing a second generation of that, and the goal there is to make it something that takes on actual data. One of the difficulties for us, of course, before this is we had no real data to base forecasts on the ACA, that we were just applying some theory. And now we are going to be getting data and looking at real data, and so we are setting ourselves up so we can take that on board.

We have also spent some time trying to talk about gaps in what we know. We have used a blog several times now to—which I kind of think of as invite the research community to help us out and do some research on some things that are gaps in our knowledge that would be helpful to us.

Senator WHITEHOUSE. My time has expired, I am sorry to say. I thank you, and I look forward to continuing our discussion.

Thank you, Chairman.

Chairman ENZI. Thank you.

Senator Grassley.

Senator GRASSLEY. I just have a couple questions.

In your testimony, you outlined work that CBO is doing to fulfill Congress' request that it incorporate macroeconomic effects into the cost estimates for major legislation. You mentioned that macroeconomic analyses requires complex modeling and takes a great deal of time. As a result, you have only been able to provide a dynamic analysis a small number of times.

Several think tanks and universities—to name a couple, Brigham Young, Wharton School—have developed their own dynamic models. I think there are others that have as well. So my question is: Has CBO reviewed these efforts to determine how it might improve its own models and increase transparency?

Mr. HALL. Sure. We have, and one of the limitations a little bit for us is those particular models you mentioned are focused on the tax side of things, and the Joint Committee on Taxation does the tax side modeling for us. So we actually are not as active on that side of things. We focused on the other side.

But, yes, we have looked at that, and I think we are going to continue to try to work with JCT to sort of understand what they are doing. And a big part of transparency to me, I think, is for us to be clear about how we are doing modeling and how the modeling is being done so we can get feedback from experts like the folks that you mentioned. It is sort of inviting criticism, but I think as long as it is in a constructive way, that is really helpful for us.

Senator GRASSLEY. Okay. Then my last question deals with Federal regulations and how they affect small businesses, farmers, and families. It has grown significantly in recent years, or at least the burden of it has. The cost of these regulations is surely impacting the entire country and our economic growth, and I notice that the CBO's latest economic outlook does not incorporate the estimated impact of the cost of regulations into its discussion of the long-term economic outlook.

Has CBO considered incorporating the cost of regulation on economic performance in your future economic forecasting?

Mr. HALL. We have not explicitly, because we have looked at sort of the historical performance of the economy and the historical performance of the budget, it is very hard to pull out the effects of regulation. It gets to be a little bit off our main focus on budgetary effects and on budget issues.

That being said, we have increased our look at regulation and regulatory effects with the eye to sort of see if there is something more that could be done to sort of help Congress in understanding regulatory burden going forward. But we do not explicitly take it

into account in our modeling, and I think that would be quite difficult to do.

Senator GRASSLEY. Could I follow up then because of your words “difficult to do”? There are organizations that I am not sure I can name that put some cost on a certain regulation or a lot of regulations and stuff like that. You are saying it is difficult. Would you say that from an intellectually accurate standpoint we should not believe too many of the other people that say regulations cost—a specific regulation or maybe a mountain of regulations is costing the economy a certain amount?

Mr. HALL. I do not mean to suggest that their work is not accurate and not a best estimate. The difficulty is for us to take this on as a burden, is the problem, I think, when I say it is very difficult. We would—

Senator GRASSLEY. Does that mean a personnel problem that you have to do it?

Mr. HALL. That is right. We are not geared up for that.

Senator GRASSLEY. Okay. Thank you.

Thank you, Mr. Chairman.

Chairman ENZI. Certainly.

Senator Toomey.

Senator TOOMEY. Thank you, Mr. Chairman.

Director Hall, thank you very much to you personally and your entire team. You and your colleagues work with my office on a regular basis, and it is a very helpful and constructive ongoing dialogue that we have, and I appreciate the work that you do.

I wanted to ask you a little bit about fair value accounting and the methodology that CBO uses as compared to the methodology that perhaps should be used. But to start with, I would just like to understand the current methodology, which my understanding is you are required not to use fair value accounting but, rather, when discounting a promised cash flow, the systematic approach of CBO is to discount that cash flow using a Treasury rate that roughly corresponds in term. Is that correct?

Mr. HALL. That is correct.

Senator TOOMEY. Is that the standard methodology?

Mr. HALL. Yes.

Senator TOOMEY. So if you use that methodology for different borrowers, is it fair to say that that methodology fails to capture the different credit quality of different borrowers?

Mr. HALL. That is right. The biggest difference I think in looking at fair value versus the so-called FCRA one is that market risk is not included, and because market risk is not included, there are things, there are elements of risk that are not being captured by that, that even the Federal Government would be exposed to, even the taxpayer would be exposed to. So the fair value we think is a bit more comprehensive estimate of the present value.

Senator TOOMEY. So an illustration for a layman to understand the flaw of using a single Treasury rate to discount projected cash flows—correct me if I am wrong. I want to understand this.

Mr. HALL. Sure.

Senator TOOMEY. If you have a loan that is made or guaranteed by the Federal Government through a vehicle like the Ex-Im Bank or more directly, and you have two loans, identical in all terms, but



in one case the borrower was a large multinational AAA corporation, and in another case the borrower is a small undercapitalized startup in a politically unstable Third World country, would you use the same discount rate to discount those identical cash flows from those very different borrowers?

Mr. HALL. I am not sure you would use the same rate for those two. Obviously, if they are borrowing from private markets, they have got to pay the market rates for borrowing. Yeah, I am not sure. I think those would like be different.

Senator TOOMEY. Under what basis? I mean, under a fair value accounting method they certainly should be discounted at different rates to reflect the very different risks.

Mr. HALL. Right.

Senator TOOMEY. And failure to do so would absolutely mislead about the nature of those risks. But in the absence of fair value accounting, what is the guiding principle that would allow you to distinguish, and what rates would you use? How would you do that?

Mr. HALL. Okay. Yeah, I am sorry to be a little vague in this. Finance is not my main area, so I am—

Senator TOOMEY. Okay. I would be happy to get a follow-up answer.

Mr. HALL. That would be good.

Senator TOOMEY. But I am concerned that we do not have an adequate mechanism, and I think CBO's hands are tied, is my understanding, into a methodology that does not sufficiently take into account the different range of credit risks that we take as a government. And to the extent that we do not take that into account, we understate the risk.

And, therefore, in the form of these assets, when they are loans, we are overstating the value of some, and we are kidding ourselves about our finances to the extent that we do that.

Now, as a general matter, my understanding is you and your colleagues have been supportive of moving to a fair value methodology because it does more accurately reflect all the risks.

Mr. HALL. That is correct.

Senator TOOMEY. But you cannot, you are not permitted to do that under existing law.

Mr. HALL. Well, we are required to do the FCRA accounting, but we often can do the fair value accounting in addition.

Senator TOOMEY. Right. And you provide that often as an addition, but it is just informative, right?

Mr. HALL. That is right.

Senator TOOMEY. And that is helpful, but it is not the official score from CBO on a given piece of legislation.

Mr. HALL. That is correct.

Senator TOOMEY. So there is a systematic risk that we are underestimating the risks of the assets that we are claiming.

Mr. HALL. That is the nature of our—we have been pretty consistent for a while now in saying that the fair value is more comprehensive because it includes more of the risk that the taxpayer really bears on—

Senator TOOMEY. Exactly. Well, thank you very much.

Mr. Chairman, I do think this is a really important item that I would like for us as a Committee to take up, if we could, simply

in the interest of having a more accurate portrayal and understanding and accounting of the risks that taxpayers takes.

Chairman ENZI. Thank you, and I will have some follow up questions on that, too.

Senator KING.

Senator KING. Thank you, Mr. Chairman. One follow-up question.

The Congressional Budget Office issued a study in December of 2015—and I think you mentioned it in your testimony—on labor market effects of the Affordable Care Act. That was widely reported as the Affordable Care Act will cost 2 million jobs or something like that.

As I read it, though, what you really found was it was the labor supply that you were analyzing, not people losing their jobs but people choosing not to stay in a particular job because they could have health insurance. Is that not correct?

Mr. HALL. That is right. It is one of the limitations. What we calculated was the idea of full-time equivalent, so we reduced hours equivalent to 2 million. That does not mean it was actually 2 million jobs. That is exactly right. It is a mix maybe of lower hours and maybe some job loss.

Senator KING. But both effects were based upon people's choices that they were likely to make not being bound to their job by their employer-supplied health insurance.

Mr. HALL. That is exactly right. So it is on the labor supply, so that is exactly right, people's incentive to work.

Senator KING. I think that is an important point, because there was a lot of talk at the time that CBO says ACA will cost 2 million jobs, and that is really not accurate.

Mr. HALL. That is correct, that we are talking about—

Senator KING. Have you done any analysis of the economic effect of people being freed from their employer based health insurance and, therefore, able to begin their own businesses, for example? I know anecdotally of people who have said that, "I have wanted to do this for 20 years. Now that I have health insurance, I can start my own business." Any studies of that?

Mr. HALL. We have not seen any, and that would be an interesting topic perhaps as time goes on and we get a little more experience with the ACA.

Senator KING. Thank you. Thank you, Dr. Hall.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Senator Whitehouse, did you have some other questions you wanted to ask?

Senator WHITEHOUSE. If you do not mind, I did want to ask one other thing.

Dr. Hall, your CBO June report, "Potential Increases in Hurricane Damage," assigned—first of all, it projected significantly higher increases in hurricane damage costs, and the report attributed about half of the growth to the effects of climate change and the other half to more development and more value in the way of the increase.

Mr. HALL. Yes.

Senator WHITEHOUSE. That focuses on hurricane damage specifically. Can you tell me about how CBO is including those climate change projections into your fiscal projections for other weather-sensitive programs, like the National Flood Insurance Program, which is probably going to be dramatically affected by the combination of storm growth and sea level rise, and various measures that either depend on sea level rise, like what do we do about Norfolk Naval Station if the sea level rises 3 feet, coastal resiliency, and then our disaster relief? That is often off budget, comes in as an emergency, but it is still a big expenditure. How are you evaluating those areas?

Mr. HALL. Well, we certainly tried to include as much of that as we could and the budgetary effect, going from the GDP effect to the budgetary effect.

Senator WHITEHOUSE. I am sorry. PDP?

Mr. HALL. GDP. I am sorry.

Senator WHITEHOUSE. GDP. Got it. I misheard you.

Mr. HALL. The effect on economic growth.

Senator WHITEHOUSE. Yeah, yeah. I thought you said "PDP," and that was not an acronym I recognized. GDP I know.

Mr. HALL. I am sorry. I am an economist. I do that. I apologize.

We did, in fact, try to look at as much of that as we could, Federal insurance and some things like that. To be honest, I am not sure about how much of all those things that you mentioned are included in that, but we did focus on the budgetary effect, and we did find that that was certainly a measurable significant effect over the next 60 years.

Senator WHITEHOUSE. Okay. Thanks very much.

Thank you, Chairman.

Chairman ENZI. Thank you.

Senator Grassley touched a little bit on the regulatory impact analysis and regulatory budget. That came up in some of our hearings that we had earlier, and I wondered if you had worked on developing a plan for how that could be done. I understand that you and your staff have had some discussions about the role that CBO might play in assessing regulatory costs of proposed rules and proposed legislation, and that you are in the process of conducting some more research into what infrastructure might be needed for the CBO to engage in this work? How is that moving forward?

Mr. HALL. Sure. Well, primarily what we focused on is the idea of how Congress can have more impact on regulatory studies and more impact on assessing the burden of regulation. And the role that CBO could play certainly it really depends upon what Congress decides they want to do, how much involvement they want.

For example, if Congress is looking for an organization to do complete studies on the effect of proposed regulation, that can take a long time, and that can be a really big deal. That would be tough to do something like that at a place like CBO, for example.

If you are looking at a place that would assess executive branch, assessment of a regulation, regulatory changes, and sort of look at it as is this something similar to what OIRA does but just something for the legislative branch, that sort of thing makes more sense.

So what we have tried to do is we have tried to focus on some of the different options Congress may have to get more involved in regulation and thinking that that is sort of the first step before we think about CBO's involvement.

One of the things that comes to my mind, for example, is if there is a large involvement, if Congress wants to get involved in a more active way, I spent some time at a place called the U.S. International Trade Commission, which is an independent commission that focuses on trade issues, and it is set up, you know, with Commissioners from both parties, and it is set up to—and it is fairly large, and it is set up to do not just assessment of trade but also particular studies on trade that Congress wants. Something like that would be an option, for example. That would be an organization that could be as big as CBO. Something smaller we could certainly take on.

One of the things that we would have to think about, of course, is if we took on almost anything, we are not geared up to do it under current staffing. So even if we did even fairly modest help, we would have to think about what sort of skills we would need to add to our skill set and maybe add some resources to that.

Chairman ENZI. Okay. Thank you.

I think this might be an area where Senator Toomey was going, because I had recently written a joint letter to the Secretary of Education about the Department's plan to issue a final rule on Federal student loans. That rule would amend existing guidelines concerning interpretation and implementation of the defense to repayment provision in the Higher Education Act. The Department estimated that its proposed rule issued in July would increase the cost of the Federal student loan programs by somewhere between \$2 billion and \$43 billion over the next decade. That is a pretty big range. How does CBO approach a matter like this when projecting costs in the next baseline? Is the Department of Education's estimate of value, or will you have to use a separate estimate to incorporate it in the baseline?

Mr. HALL. We will, and we always perform our own estimates. So we would probably take a look at what they have done, but we would perform our own analysis and come to our own conclusions about the likely impact and whether that—and discuss about incorporating that into the baseline if it is not already there. That is something that we wind up doing all the time as it is, and we always do our own independent analysis of things like this.

Chairman ENZI. To get back to what Senator Toomey was asking about, would that have some of these risk factors in it as well? Or does that fit within what CBO does?

Mr. HALL. You mean the risk factors are in how much uncertainty there is and—

Chairman ENZI. On different student loans, whether they will be repaid or not.

Mr. HALL. Oh, yes, yes. Certainly we try to take the risk factor, obviously, into account. I am not sure we do a present value sort of analysis of this, but we would probably come up with a point estimate and revisit it as experience allows and try to communicate somewhat the uncertainty, the risk involved in the estimate.

Chairman ENZI. One proposal that I have heard out there—and I do not know who it was from—was that if students complete their college degree and there is not a job in that field, they should be able to sue the Federal Government for forgiveness of their loan. That would be a new risk factor, I assume.

Mr. HALL. Well, that is right, and we would try to forecast that.

Chairman ENZI. Yes. So would you have to look at what majors they have? [Laughter.]

That is not a fair question. I do not have any more questions. Senator Whitehouse, do you have any other questions?

Senator WHITEHOUSE. Nor do I. Thank you, Chairman.

Chairman ENZI. Thank you, Dr. Hall, for being here and for your answers. And if anybody has any additional questions they want to submit, they can do that, but they should be turned in by 5 o'clock tomorrow night, and we would appreciate it if you would answer those, plus there were a few that we needed follow-up on from the questions that were given already.

Mr. HALL. Absolutely. Thank you.

Chairman ENZI. Thank you very much. This hearing is adjourned.

[Whereupon, at 4:31 p.m., the Committee was adjourned.]



## Congressional Budget Office

NOVEMBER 18, 2016

### Answers to Questions for the Record Following a Hearing on the Oversight of the Congressional Budget Office Conducted by the Senate Committee on the Budget

*On September 14, 2016, the Senate Committee on the Budget convened a hearing at which Keith Hall, Director of the Congressional Budget Office, testified about CBO's work since May 2015 and its plans for the future ([www.cbo.gov/publication/51923](http://www.cbo.gov/publication/51923)). After the hearing, Chairman Enzi, Ranking Member Sanders, and other Members of the Committee submitted questions for the record. This document provides CBO's answers.*

#### Chairman Enzi

**Question.** Last week, Deputy CBO Director Mark Hadley testified before the House Budget Committee on the budgetary effects of the Center for Medicare & Medicaid Innovation (CMMI).<sup>1</sup> Significant concerns were raised in that hearing by members of the Committee and by the other witnesses about the assumptions and models used by CBO.

One of those witnesses, Joseph Antos, a scholar at the American Enterprise Institute and former Assistant Director for Health and Human Resources at CBO, highlighted the importance of CBO's "decision to account for savings that might be lost for 'initiatives CMMI is undertaking (or is expected to undertake)' in assessing legislative proposals." Mr. Antos testified that, "This remarkable decision to score lost savings for demonstration projects that have yet to be announced is a sharp break with past practice." He goes on to suggest, "Just as CBO does not score legislative proposals that have not yet been advanced, it seems unreasonable for them to score actions by CMMI that have not yet been advanced." Can you please explain CBO's rationale for making this decision? Please describe the criteria, data sources, and process CBO uses to determine whether CMMI is likely to undertake any future demonstration.

**Answer:** CBO's estimate that CMMI's activities will reduce federal spending over the next decade is based primarily on judgments about the effectiveness of the center's process for conducting demonstrations, not on judgments about the expected results of particular demonstrations that the center is conducting or likely to conduct in the future. On the basis of evidence from earlier periods, CBO expects that a small share of the demonstrations conducted by CMMI will achieve savings, most will have little or no effect on federal spending, and some will increase spending. A crucial feature of the legislation that

1. Testimony of Mark Hadley, Deputy Director, Congressional Budget Office, *CBO's Estimates of the Budgetary Effects of the Center for Medicare & Medicaid Innovation* (September 7, 2016), [www.cbo.gov/publication/51921](http://www.cbo.gov/publication/51921).

established CMMI is that it authorizes the Secretary of Health and Human Services to expand demonstrations under the following circumstances: when they are expected to decrease federal spending without harming quality of care or when they are expected to improve quality without increasing spending. The savings that CBO expects to result from CMMI's activities would stem largely from the expansion of demonstrations that reduce spending.

Because the expected savings from CMMI's activities are incorporated in CBO's baseline projections of federal spending, CBO must consider the implications for those savings when estimating the cost of legislative proposals that would interact with the center's activities. Many such proposals are of two types: those that would require the center to take actions that overlap with those that it might take under current law (such as requiring the center to conduct particular demonstrations) and those that would prevent the center from taking certain actions (such as prohibiting specific demonstrations).

For legislative proposals that would require CMMI to take certain actions, CBO assesses the likelihood that the center would have taken similar action under current law. CBO obtains detailed information on the features of demonstrations that have been announced or are under way from CMMI's website. To monitor the center's plans for future demonstrations, CBO routinely gathers information from publicly available sources such as CMMI's Requests for Information—in which the center solicits input from providers and other stakeholders about the design of demonstrations under consideration—as well as from public statements and presentations by Administration officials. CBO also consults staff at CMMI and various stakeholders.

In assessing the degree of overlap between a legislative proposal and CMMI's activities, CBO accounts for how much interest the center has shown in testing similar approaches—either in terms of the tools that would be used or in terms of the opportunities for savings that would be targeted. An example of tools would be the management of prescriptions before a hospital discharge, and an example of opportunities targeted for savings would be avoiding hospital readmissions. CBO looks at both tools and targets because, even though multiple tools may address the same problem, the resulting savings can often be realized only once. For instance, many approaches may try to reduce hospital readmissions, but a given readmission can be avoided only one time. If a proposal required CMMI to conduct a demonstration that aimed to reduce hospital readmissions, CBO would have to determine if other demonstrations were already trying to achieve that goal and the chances that the resulting savings were already accounted for in the agency's baseline projections.

In some cases, proposals requiring actions that overlap with those that CMMI might have taken anyway would increase federal spending. For example, a proposal to limit CMMI's flexibility in designing and refining a demonstration could decrease savings, in CBO's judgment, by reducing the likelihood that it would succeed or, if it did succeed, the magnitude of expected savings. In other cases, proposals that interact with CMMI's efforts would reduce federal spending. For example, if CBO has enough information to estimate that a particular demonstration would probably reduce spending, a legislative proposal to implement it faster than CMMI had planned would reduce spending, in CBO's judgment, by enabling the government to achieve savings sooner than it would have otherwise.

Similar considerations apply to legislative proposals that would prevent CMMI from taking certain actions. However, because the next question deals specifically with proposals to prevent CMMI from conducting particular demonstrations, CBO's approach to evaluating such proposals is covered in the response to that question.

**Question.** CBO currently estimates CMMI will reduce federal spending, on net, by \$34 billion from 2017–2026 (with CMMI spending an estimated \$12 billion on demonstration projects that would reduce spending on Medicare benefits by approximately \$45 billion in total over the 10-year period). In his prepared remarks, Mr. Hadley stated that CBO's estimate is "based on judgments of how effectively the center will identify, refine, and expand approaches that reduce spending" but then later admits that such judgments are inherently uncertain.

Mr. Hadley observed that CBO's estimates for CMMI spending are more straightforward than its estimates of any potential reduction in spending resulting from the center's activities. Mr. Hadley indicated CBO's assessment is "primarily based on judgments about the effectiveness of the process, not on judgments about the expected results of particular demonstrations." Rather, CBO's estimates are based on sets of demonstrations and the assumption that HHS will expand successful demonstrations and that those expansions will, in turn, reduce federal spending.

If CBO doesn't base its CMMI estimates on particular demonstrations—but rather a set of demonstration projects with the assumption that the center has the broad authority to identify, modify, or expand approaches such that it will ultimately be successful in pursuing demonstrations that reduce spending—and if there is a high degree of uncertainty about whether any particular demonstration will yield savings without harming quality, then why should Congress be penalized for preventing a particular project from being pursued? Based on how CBO constructed its estimates for CMMI, and its resulting effects on the baseline for Medicare spending, why wouldn't CBO simply assume that CMMI would have the ability to identify and fund another demonstration that is equally as likely to succeed over time?

Mr. Hadley's testimony goes on to explain that "When asked to estimate the cost of a legislative proposal that would prevent the center from conducting a specific demonstration project, CBO assesses how much is known about the potential budgetary effects of that demonstration ... When CBO does have a basis for estimating how a specific project would affect federal spending, the agency incorporates that information into its estimate." Considering the explanation from Mr. Hadley's testimony above, can you please explain why CBO's current method for scoring policy proposals is biased against legislative changes made by Congress?

If savings from a particular CMMI demonstration are not specifically included in CBO's baseline then how is it consistent or fair to assume that blocking a particular demonstration in a set would produce a cost relative to a baseline which does not include the individual budgetary effects of the demonstration that is being blocked in the first place? Is there a double standard that is being applied in this scenario?

**Answer.** To analyze legislative proposals that would prevent CMMI from conducting a particular demonstration, CBO first assesses how much is known about the potential budgetary effects of the demonstration. The agency bases such assessments on a careful review of available research and other relevant information. When CBO has a basis for estimating how a specific project would affect federal spending, the agency incorporates that information into its estimate. For example, CBO recently used that approach to estimate the cost of a bill to prevent the Secretary of Health and Human Services from implementing a proposed



demonstration that would modify the method used to pay providers for prescription drugs covered under Medicare Part B.<sup>2</sup>

For most demonstrations that have not yet been tested, CBO has no basis for judging how conducting or preventing that particular demonstration would change federal spending. Because CBO expects that CMMI's overall process of testing, evaluating, and expanding demonstrations will produce savings, on average, proposals that prevent demonstrations from occurring would tend to reduce those average savings and thus increase spending. CBO's projections of the budgetary effects of CMMI are based on an estimate of the percentage reduction in federal spending that will be achieved, on average, from the set of demonstrations that begin each year. That projected reduction in federal spending results mainly from the expansion of demonstrations that save money, which CBO expects will represent a small share of the demonstrations conducted by CMMI. Because CBO has no basis for predicting which particular demonstrations in a set will be found to reduce spending, a proposal to prevent a specific demonstration from occurring reduces the expected savings from that set of demonstrations.

In estimating the cost of a proposal to prevent a demonstration, CBO anticipates that CMMI would pursue one or more alternative projects that also have the potential to achieve savings. Because developing and implementing those replacements would take time, CBO would account for that delay when estimating the cost of such a proposal. The agency would also consider atypical features of the prohibited demonstration (such as its size), the possible effects on the willingness of health care providers to participate in the development of similar demonstrations that might ultimately be blocked, and other factors.

In creating CMMI, the Congress gave the Department of Health and Human Services (HHS) the authority to take various actions that CBO estimates will reduce spending, on average. In general, proposals that block HHS from taking such actions are expected to increase spending, on average. In CBO's view, that conclusion is not a result of bias but a consequence of the authority that the Congress gave to HHS.

**Question.** How, if at all, might CBO alter its estimates for CMMI to take into account the potential that the center may attempt to implement or expand a particular demonstration project that it does not have the statutory authority to pursue as planned? Would CBO use probabilistic scoring in such a scenario? If so, how would it affect CBO's baseline or the cost estimate for a legislative proposal by Congress to prevent a potentially unlawful demonstration from moving forward as planned?

**Answer.** CBO bases its projections of the budgetary effects of CMMI's activities on the anticipated budgetary effects of how the Administration will use the authorities available in current law, not on analyses of how the legislative or judicial branches of government might view that use. Therefore, CBO's baseline projections incorporate the expected effects of the Administration's actions. If the Congress acts to modify those actions, CBO will estimate the budgetary effect of that modification. That estimate would depend on the specifics of the proposed change.

2. See Congressional Budget Office, cost estimate for H.R. 5122, a bill to prohibit further action on the proposed rule regarding testing of Medicare Part B prescription drug models (October 4, 2016), [www.cbo.gov/publication/52087](http://www.cbo.gov/publication/52087).

**Question.** CBO has indicated that it is monitoring CMMI's implementation of demonstrations and will update Congress with its assessments as more information becomes available. However, in his testimony before the House Budget Committee, Mr. Hadley stated multiple times that at this point there is little information available to CBO to update its estimates. CBO indicated that "many of the demonstrations initiated by the center are in their early stages, and evaluation reports are not yet available for all of them."

When does CBO expect to have sufficient data to update and revise its estimates? When will CBO inform Congress of its updated assessment of CMMI? How might CBO's baseline and the models and assumptions it relies on to produce its CMMI estimates change going forward?

Mr. Hadley also noted that "CBO has limited information about the standards that Medicare's Chief Actuary will use in certifying that demonstrations may be expanded." If CBO has limited information regarding the CMS Actuary's certification then how can the agency be so confident that the demonstration projects expanded by the HHS Secretary are likely to reduce spending?

**Answer.** Over the next several years, CBO expects to learn much more about CMMI's activities and will use that information to improve its budget projections. During that period, CBO will keep the Congress apprised of any changes to its estimates. To improve its projections, CBO will continue monitoring all aspects of CMMI's activities, including its approach to selecting, testing, and evaluating demonstration projects. CBO will pay particular attention to evaluation reports that are released and decisions by HHS about whether or not to expand some demonstrations—and the projected savings from those that are expanded. However, it is not possible at this time to determine how CBO's estimates of the budgetary effects of CMMI's activities might change as a result of that new information.

CBO's assessment of the budgetary effects of CMMI's activities involves judgments that are inherently uncertain. As noted in response to an earlier question, CBO's projections of the budgetary effects of CMMI are based on an estimate of the percentage reduction in federal spending that will be achieved, on average, from the set of demonstrations that begin each year. That projected reduction in federal spending comes mainly from the expansion of demonstrations that save money, which CBO expects will represent a small share of the demonstrations conducted by CMMI. CBO anticipates that the Secretary of Health and Human Services will expand some models that are expected to reduce federal spending while maintaining or improving quality and other models that are expected to improve quality without increasing spending. The Chief Actuary of the Centers for Medicare & Medicaid Services must certify the expected effects on spending before the expansion may proceed.

CBO expects that, in making decisions about whether to certify that certain models would not increase federal spending if expanded, the Office of the Actuary will base its determinations on a combination of the following: the findings of demonstration evaluations, the findings of prior research, and its own analysis. CBO expects that the Office of the Actuary will use reasonable approaches to make its determinations and that it will be successful in identifying demonstrations that could clearly be expected to increase spending. Because the results of the evaluations will play a crucial role in making those determinations, CBO will monitor those findings as well as the evaluation process, including the rigor of the research methods used to evaluate demonstrations. That information will help CBO improve its budget projections.

**Question.** Recent testimony you have provided to this Committee and to the Appropriations Committee discusses the impact of the limits of the compensation CBO can pay individual staff members, contrasting it with the higher limits often available to executive branch agencies. Yet when I asked you in writing in May 2015 for specific information concerning compensation paid to CBO employees, you withheld certain data on the grounds that it constituted “sensitive personnel information.” Notably, my request did not ask for individually identifiable information.

Earlier this year, the House Oversight and Government Reform Committee asked for—and received—multi-year performance award bonus data from the Office of Personnel Management and several other executive branch agencies, with the data broken down by employee titles and salary grades. I do not understand why CBO is unable to provide the same level of information to this Committee. Therefore, I ask that you provide full responses to my inquiries of May 2015 related to compensation paid by CBO in which your earlier responses indicated that certain data was withheld on the grounds that it constituted “sensitive personnel information.”

**Answer.** In May 2015, Chairman Enzi asked a series of questions related to performance bonuses awarded by CBO: How many of those bonuses are awarded each year? What is their average size? Are there written guidelines about how they are awarded, including a specified maximum bonus (either in dollar terms or as a share of base salary)? Is the entire sum intended for performance bonuses awarded each year, or are some of those funds allowed to lapse?

CBO expects strong performance from its employees, and the agency’s compensation policies are designed to attract and retain the best possible employees and to reward them, to the extent feasible, for outstanding work. To that end, each year, CBO’s budget request includes an allocation for cash bonuses, and once the appropriation is set, the Director determines whether the agency can provide such bonuses. If it can, the Director determines the amount that can be devoted to them and the guidelines—which are communicated in writing in some years and orally in others—for allocating them. The Director also makes the final decision about each bonus paid to a CBO employee.

CBO’s budget for performance bonuses has varied from year to year. The agency has paid bonuses in four of the past five years—to roughly half of the staff each year (see Table 1). During fiscal year 2013, CBO did not pay any cash bonuses because of budget constraints (though the agency did award some employees extra time off instead). In the past three years, CBO did not use its entire budget for bonuses.

**Question.** According to the Congressional Research Service, there are 87 federal programs that provide assistance to low-income individuals or communities. Despite their common purpose of assisting the poor, most of these programs have different eligibility criteria related to income, assets, and household composition. These differences are administratively complex and result in disparate treatment of similarly situated individuals.

As I understand the process, most CBO analysts develop their own models to create baselines and score legislative proposals. These models are specific to each program; and they reflect federal spending in the states on a combined basis. However, in the area of welfare there are many interrelated programs with unique state level differences. The ability to model these programs would seem to call for a microsimulation model like the one developed for HHS by the Urban Institute, the so-called TRIM3 model.

Table 1.

**Performance Bonuses at CBO**

	2012	2013	2014	2015	2016
Total Number of Awards	125	0	114	119	118
Mean Award (Dollars)	4,452	0	5,004	4,466	4,746
Median Award (Dollars)	4,000	0	5,000	4,000	5,000

Source: Congressional Budget Office.

Years indicated are fiscal years.

Does CBO have the ability to develop such a model, or given the time and resources involved, would it be more cost effective to use the HHS model? Would HHS provide CBO with access to their model?

**Answer.** Though CBO maintains program-specific models that are used to forecast spending and estimate the budgetary effects of proposed changes in law, that approach does not prevent the agency from considering whether legislative proposals directly affecting one program would indirectly affect other programs. For example, CBO models Medicare and Medicaid separately. Nevertheless, when a proposal would directly affect people's eligibility for Medicare and as a result affect Medicaid spending indirectly, CBO accounts for that indirect effect.

CBO could develop a microsimulation model that examined the interrelated programs that provide assistance to low-income people or communities. However, doing so would require a significant commitment of time and resources, and it is not clear that the results from such a model would differ substantially from the results of CBO's current processes. Because the overall demand for CBO's work is high and because its resources are limited, the agency would need to balance such a commitment with its other responsibilities.

The model developed and maintained by the Urban Institute would not be adequate for CBO's needs and could impair CBO's work in some ways. The model can only examine history; it cannot make projections, so it could not be used by itself to create baselines or to estimate the budgetary effects of legislative proposals. Moreover, CBO's work has to reflect the agency's objective, impartial, and nonpartisan analytical judgment. Reliance on a model developed for a Cabinet department to inform its policy recommendations would impair that practice and might raise questions about CBO's objectivity. In addition, CBO works hard to make its analysis transparent so that Members of Congress, their staff, and outside analysts can understand the agency's results and question its methods. That practice too would be impaired, because CBO's ability both to understand and to explain the results of a model run by the Urban Institute would probably be limited.

**Question.** CBO uses several private-sector forecasting models to estimate short-run "demand-side" effects. It uses two of its own models to estimate long-run "supply-side" effects. Results from the short-run and long-run models are essentially spliced together in an ad hoc manner to produce ten-year dynamic estimates. Professor John Taylor at Stanford University has

suggested the use of a single integrated model like the one used by the European Central Bank (ECB).

Has CBO reviewed the ECB model and considered whether such an integrated model might produce more consistent results?

**Answer.** CBO uses a range of empirical results and economic models, rather than any single result or model, to develop its estimates. The agency therefore keeps abreast of advances in macroeconomic modeling, including improvements in dynamic general equilibrium (DGE) models like the model used by the ECB.<sup>3</sup> Such models are firmly grounded in economic theory and provide a unified framework for short-term and long-term macroeconomic analysis, but they often require a large number of very specific assumptions about households' behavior, firms' behavior, and future government policies. Furthermore, their predictions can vary widely with those assumptions. And the relationships between the assumptions and the resulting predictions are often difficult to explain.

CBO's current practice—using a clearly defined rule to merge the estimates from short-term and long-term models—is both transparent and easy to use. It is informed by a large economics literature, including research based on DGE models.<sup>4</sup>

#### Ranking Member Sanders

**Question.** CBO's report on the changing distribution of family wealth since 1989 was staggering. As the report makes clear, since the 1980s there has been an enormous transfer of wealth from the middle class and the poor to the wealthiest people in this country. There is something profoundly wrong when the rich keep getting richer and virtually everyone else gets poorer.

From 1989 to 2013, the wealth of families in the top 10 percent increased by 153 percent. Meanwhile, the wealth of the bottom 50 percent of families has declined by 19 percent. In 2013, families in the bottom 25 percent were \$13,000 in debt, on average, whereas they had virtually no debt in 2001. A total of 15 million families were in debt in 2013, with an average indebtedness of \$32,000.

I have to imagine that the growing number of people in debt reduces both consumer spending, which represents 70 percent of our GDP, as well as tax collection, as the growing number of people with little income and no wealth do not pay much in federal taxes.

What are the economic and budgetary effects of this enormous growth in wealth inequality?

In addition, what type of analyses on wealth and income inequality is CBO planning on conducting in the future?

3. For a detailed discussion of DGE models and their advantages and disadvantages, see Felix Reichling and Charles Whalen, *Assessing the Short-Term Effects on Output of Changes in Federal Fiscal Policies*, Working Paper 2012-08 (Congressional Budget Office, May 2012), [www.cbo.gov/publication/43278](http://www.cbo.gov/publication/43278).

4. See Congressional Budget Office, *How CBO Analyzes the Effects of Changes in Federal Fiscal Policies on the Economy* (November 2014), [www.cbo.gov/publication/49494](http://www.cbo.gov/publication/49494).

**Answer.** CBO is not aware of any research that draws a definitive link between the concentration of wealth and economic growth or between the concentration of wealth and the federal budget. However, the concentration of wealth is likely to affect the federal budget only slightly, either by changing revenues or by changing spending. Wealth is not a significant part of the federal tax base, so any effects of changes in the distribution of wealth on revenue would probably be small. And though assets help determine people's eligibility for some federal programs, changes in the distribution of wealth are unlikely to change overall federal spending significantly.

More research has been performed on the link between the concentration of income and economic growth, though the conclusions of that research are uncertain. Some studies conclude that income inequality leads to faster growth, others that it slows growth, and still others that it does not affect growth. Therefore, CBO's projections of economic growth do not explicitly include any effects of changes in income inequality. However, those projections are based on historical evidence, so they implicitly include some effects of income inequality—to the extent that past changes in inequality have affected economic growth.

Research has also been performed on the relationship between income inequality and federal revenues, which is better understood. For instance, revenues from individual income and payroll taxes depend on the distribution of income—which, in turn, depends on the distribution of earnings from wages and salaries. CBO's projections reflect an expectation that those earnings will grow faster for higher-income people than for others during the next decade, as they have over the past several decades. That difference would cause a larger share of income to be subject to higher tax rates, and revenues from individual income taxes would consequently grow. Payroll tax receipts would decline, however, because more earnings would be above the threshold beyond which they are not taxed for Social Security.

CBO would welcome the opportunity to discuss its research priorities, including the extent to which future work on the distribution of wealth or income should be one of those priorities.

**Question.** Social Security is a lifeline keeping millions of seniors, disabled and their families out of poverty.

Social Security has a \$2.7 trillion trust fund, but rising income inequality is constraining the program's ability to raise the level of revenue that we could expect if the income inequality gap were narrowing. The last time Social Security underwent major changes, in 1983, the payroll tax cap was set to cover 90 percent of all earned income. No one at that time imagined the explosion in inequality would see those at the very top capturing so much of our economic gains over the past three decades. The Center for American Progress has found that this rise in income inequality has already cost the trust fund more than \$1.1 trillion.

Today, CBO projects that that income inequality will continue to rise, leaving only 78 percent of earned wages under the payroll tax cap by the end of its projections.

According to the 2016 Social Security Trustees Report, Social Security will be able to pay every benefit owed to every eligible beneficiary until the year 2034. After that date, Social Security will still be able to pay about 75 percent of benefits to every eligible beneficiary.

However, CBO projects that the combined Social Security trust funds will not be able to pay 100 percent of earned benefits to beneficiaries by 2029—five years before the Social Security actuaries estimate.

Does CBO's estimate of the increase in income inequality explain part of this difference between CBO's projections and estimates from the Social Security Actuary? If so, how much?

**Answer.** CBO's projections of the amount of earnings subject to the Social Security payroll tax are derived from the agency's projections of the distribution of compensation. Those projections reflect CBO's expectation that earnings will grow faster for higher-income people than for others during the next decade—as they have over the past several decades—and that the earnings of all taxpayers will grow at similar rates thereafter. By contrast, the Social Security Trustees' projections of taxable earnings suggest that they expect earnings to grow at similar rates for all earners during the next decade. In other words, CBO expects greater inequality in earnings than the Trustees do.

If CBO adopted the Trustees' projections of taxable earnings—specifically, their projections of the share of earnings subject to the payroll tax, of the share of total compensation paid as earnings, and of compensation as a share of gross domestic product (GDP)—but did not allow those changes to affect CBO's projections of other factors, the agency's estimates of payroll tax receipts, and eventually of benefits paid, would rise. As a result, CBO's projection of Social Security's 75-year actuarial balance would improve from –1.55 percent of GDP to –1.41 percent, a difference of 0.14 percent of GDP. That difference would account for about a quarter of the difference between CBO's and the Trustees' projections. The strongest factor in that change would be the higher projection of the share of earnings subject to the payroll tax. Adopting the Trustees' projections of taxable earnings would also change CBO's projection of the exhaustion date of the combined Social Security trust funds by two years, from 2029 to 2031.

Adopting the Trustees' projections of taxable earnings would affect other aspects of CBO's budget projections as well. For example, individual income tax receipts would fall more than payroll tax receipts would rise.

**Question.** I found CBO's work on the budgetary impact of the increased severity of hurricanes due to climate change to be extremely helpful. However, the analysis only dealt with the projected increase in discretionary spending. As the impacts of climate change increase, mandatory spending will increase as well—federal flood and crop insurance programs are just two examples. In fact, GAO placed the federal government's fiscal exposure to the effects of climate change on its “high risk” list.

With these facts, and CBO's access to new analytical tools, how are you incorporating the financial risks of climate change exposure into your baseline? What further analyses beyond this year's hurricane paper is CBO considering?

**Answer.** Under the rules governing baseline projections, some of the potential budgetary effects of climate change can be reflected in the baseline, but some cannot. Some of the programs most affected by weather-related disasters, such as federal crop insurance and flood insurance, are mandatory spending programs. For those programs, CBO attempts to

incorporate into its projections all factors that might affect spending under current law—including land use and crop yields, which may be affected by climate change.

But CBO is required to apply a different treatment to discretionary spending that is affected by weather-related disasters, such as spending by the Disaster Relief Fund operated by the Federal Emergency Management Agency. In CBO's 10-year baseline projections, as specified in law, the amount of discretionary funding appropriated for a particular program in the current year is assumed to be provided in each subsequent year, with adjustments for inflation. The baseline therefore incorporates the assumption that funding for disaster relief in each year of the coming decade will be similar to the amount that was provided for the current year. (The baseline also incorporates the assumption that total discretionary appropriations are constrained by the caps imposed by the Balanced Budget and Emergency Deficit Control Act of 1985, as amended.)

The Congress has typically responded to large-scale weather-related disasters, such as Hurricanes Katrina and Sandy, by enacting legislation to increase spending—providing emergency supplemental appropriations for disaster relief, for example. In the future, lawmakers might spend more than projected in CBO's baseline if climate change made weather-related disasters more severe or more frequent. For example, increased damage from storm surges might lead the Congress to pass additional emergency supplemental appropriations for disaster relief or to provide funding to protect vulnerable infrastructure. But following the rules that govern baseline projections, CBO does not attempt to predict the Congress's response to such events. Alternatively, the Congress might amend existing laws in order to limit federal spending on weather-related disasters—for instance, by increasing the share of postdisaster assistance for which states and localities are responsible. But CBO's baseline projections are built on current law, so they cannot incorporate assumptions about such possible changes.

Climate change may also affect the nation's economic output and consequently affect federal tax revenues. However, researchers estimate that those effects will probably be very small in the near future. For example, one recent study found that over the 2020–2039 period, the effect of climate change on outdoor workers' productivity would probably be between an increase of 0.03 percent and a decline of 0.38 percent. (Such estimates are very uncertain.) In addition, CBO has concluded that changes in the frequency of major hurricanes could have persistent negative effects on economic output, but only if climate change were to make such storms frequent enough that the economy might not fully recover from one catastrophic storm before it was hit by another. In contrast, CBO has concluded that, over the long run, a single hurricane would have no significant impact on the nation's GDP. That conclusion reflects the fact that, in the long run, GDP is determined by the size of the capital stock (which is determined by capital across the country, national saving, and capital inflows, none of which are likely to be permanently affected by one hurricane) and by the labor supply and technological progress (which also are not likely to be permanently affected).

In addition to its recent report about hurricane damage and the federal budget, CBO is currently examining the fiscal viability of the National Flood Insurance Program.<sup>5</sup> That analysis draws upon the most recent estimates of flood risk under current conditions. CBO is also assessing the federal crop insurance program, making a qualitative analysis of factors that

5. The recent report is Congressional Budget Office, *Potential Increases in Hurricane Damage in the United States: Implications for the Federal Budget* (June 2016), [www.cbo.gov/publication/51518](http://www.cbo.gov/publication/51518).



affect the government's budgetary costs, such as weather and the potential long-term implications of climate change.

**Question.** The costs of failing to address basic environmental and public health protections is immense. We spend hundreds of millions or even billions of dollars a year on completely preventable health impacts, such as elevated cancer rates due to the exposure of toxic chemicals and respiratory problems, heart attacks, and strokes cause by ozone pollution from power plants and vehicles. For instance, a new study published in the *Journal of Public Health Policy* found that bacterial infections tied to contaminated water systems cost Medicare an average of \$600 million a year between 1991 and 2006, with costs continuing to rise. Many of these costs are borne by federal programs, such as Medicare, Medicaid, and the VA, while other costs are borne through higher premiums for private health insurance plans.

How can you begin to incorporate these costs into your scoring methodologies?

**Answer.** Some of the health care programs most affected by the health of the population are mandatory spending programs. For those programs, CBO attempts to incorporate into its baseline projections many factors that might affect spending under current law—including changes in the composition of the population, changes in health care prices, and changes in the quantity of services used. The budgetary effects of other factors, such as existing threats to public health, are reflected in CBO's baseline projections because the projections are based partly on current spending and recent trends in spending.

Taking such costs into account when estimating the budgetary effects of legislation that would address environmental or public health concerns would be challenging, however. Little research has been done on the budgetary effects of policy interventions aimed at reducing pollution and other threats to public health. Furthermore, the effects of such policies on overall health care spending and on health outcomes that directly affect the federal budget, such as disability and longevity, are not well understood. Some of the questions that CBO would need to answer in order to account for those effects in a cost estimate include the following:

- How much pollution would be reduced by a particular policy proposal, and over what period?
- How would changes in pollution affect health?
- How would any improvements in health affect health care spending and life expectancy?

Federal outlays (including outlays for Social Security, Medicare, and Medicaid) would also be affected if policies addressing environmental hazards eventually led to lower disability rates or greater longevity. Lower disability rates could reduce outlays; greater longevity could increase them. But those outcomes are highly uncertain, and further research on the potential long-term effects of such policies would be beneficial.<sup>6</sup>

6. For more information about how CBO analyzes the effects of changes in health on the federal budget, see Congressional Budget Office, *Raising the Excise Tax on Cigarettes: Effects on Health and the Federal Budget* (June 2012), [www.cbo.gov/publication/43319](http://www.cbo.gov/publication/43319).

**Question.** CBO's analysis of income in America, released this June, leaves out potentially hundreds of billions of dollars of income going to the very wealthiest households. CBO states in the appendix of the report that it excludes from its definition of income "increases in the value of assets that have not been realized through sales."

This means that the increase in value of an asset is included in income only when that asset is actually sold. Unrealized capital gains do appear as changes in wealth in CBO's analyses of wealth, but do not appear in CBO's analyses of income even though such gains are income in a real and practical sense.

CBO concludes that the richest 1 percent of American households received 17 percent of market income in 2013 and paid an average federal tax rate of 34 percent that year.

These figures would be different if CBO's definition of income included unrealized capital gains, which largely flow to the richest Americans. The estimated share of income going to the richest one percent would be higher, and the estimated average federal tax rate for the richest one percent would be lower.

Can you tell us how different CBO's distribution of income and average tax rates for different income groups would be if it included unrealized capital gains in its definition of income?

**Answer.** CBO has not estimated how the distribution of income or the distribution of average tax rates would change if unrealized capital gains were counted as income. One reason is that such a calculation, to be precise, would require data about year-to-year changes in the value of assets, including assets that have not been sold—and such data are not readily available for representative samples of the population.

Some researchers have tried to estimate capital gains as they accrue by using assumptions about annual rates of appreciation of assets held by households at different income levels.<sup>7</sup> Their research suggests that the share of income, including unrealized capital gains, going to the highest-income households may be larger than the share of income, excluding such gains, that CBO has estimated in years when asset values have risen—and smaller in years when asset values have fallen. However, those researchers do not estimate what average tax rates (including the effect of accrued tax liabilities on unrealized capital gains) would be if income were defined as including unrealized capital gains.

A second problem with counting unrealized capital gains as income is that it would create an inconsistency between the accounting principles used to measure income and those used to measure federal taxes. The income tax system levies taxes on income from the appreciation of assets only when the owner sells the asset and realizes the gain. In counting realized but not unrealized capital gains in its measure of income, therefore, CBO is following the accounting principles of the tax system.

7. See Philip Armour, Richard V. Burkhauser, and Jeff Larrimore, "Levels and Trends in U.S. Income and Its Distribution: A Crosswalk From Market Income Towards a Comprehensive Haig-Simons Income Approach," *Southern Economic Journal*, vol. 81, no. 2 (October 2014), pp. 271–293, <http://dx.doi.org/10.4284/0038-4038-2013.175>. For an alternative approach that reaches different conclusions about the effect of accrued capital gains on levels and trends in income inequality, see Timothy M. Smeeding and Jeffrey P. Thompson, "Recent Trends in Income Inequality," in Herwig Immervoll, Andreas Peichl, and Konstantinos Tatsiramos, eds., *Who Loses in the Downturn? Economic Crisis, Employment and Income Distribution*, vol. 32 of *Research in Labor Economics* (Emerald Group Publishing, 2011), pp. 1–50, <http://tinyurl.com/qdk92x4>.

Including unrealized capital gains in estimates of wealth, by contrast, does not create such an inconsistency. Wealth is a measure of the economic resources that a household holds at a point in time. CBO's measure of wealth does include unrealized capital gains, so it is effectively an estimate of the income available to a family if it were to liquidate its assets immediately. But the data that CBO uses for that analysis capture only the cumulative value of unrealized capital gains, not the year-to-year change in that value.

**Question.** In February, the Government Accountability Office (GAO) issued a report detailing that the way the federal government has done budgeting for over 25 years—through the Federal Credit Reform Act or FCRA—is the most appropriate way to estimate the cost of our vital credit programs. The report also found so-called “fair value accounting” is in fact not appropriate for estimating subsidy costs to the federal government.

Fair value accounting inflates the costs of federal loan and loan guarantee programs. For example, under the appropriate FCRA accounting, the government turns a profit of \$81 billion over ten years on federal student loans. Under fair value accounting, our loan programs are estimated to cost the government more than \$146 billion over this time period. (Neither of these figures include administrative expenses.)

Fair value accounting unnecessarily adds an additional private-sector risk factor to our public student loan program. This is inappropriate because federal student loans are backed by the full faith and credit of the United States, and the federal government can use every tool of law our country has to collect this debt. And unlike a small lender, any year-to-year volatility of repayments won't bankrupt the federal government. Moreover, there is no risk premium placed on other federal programs that may go over budget such as the Defense Department's F-35 Joint Strike Fighter program.

Given GAO's report, the fact that FCRA already takes into account the expected risk to the federal government of students defaulting on their loans, and the fact that students loans are an extremely safe bet for a return on investment to the federal government do you think it is at all reasonable for CBO to continue to call for switching to fair value accounting for this and other credit programs? Is GAO wrong in its conclusion that FCRA is the most accurate and therefore most appropriate tool to estimate the budgetary cost to the federal government of credit programs?

**Answer.** CBO has stated in much of its published work that fair-value estimates provide a more comprehensive measure of the cost of federal programs than the estimates required by FCRA do. The agency has also stated that fair-value estimates would more closely align the federal government's evaluations of its risk with the public's evaluations of that risk.<sup>8</sup> However, CBO has not taken a position on whether and to what extent fair-value estimates should be

8. The gains or losses from taking on such risk are ultimately passed on to the public through changes in tax and spending decisions. Some economists note that the federal government can borrow money, often at low interest rates, in periods when the economy is weak in order to avoid having to immediately raise taxes or cut spending to offset a loss in a particular program. Therefore, they argue, the government's ability to borrow at low rates mitigates the cost of market risk. However, such borrowing is effectively a separate decision about the path of future taxes and spending and thus should not be attributed to a present-value estimate of the cost of a program, in CBO's judgment. See Congressional Budget Office, *Fair-Value Accounting for Federal Credit Programs* (March 2012), [www.cbo.gov/publication/43027](http://www.cbo.gov/publication/43027).

used instead of FCRA-based estimates. Both types are forms of accrual accounting; that is, they recognize the cost of an activity in a single up-front amount in advance of the actual cash transactions that will follow.

Budget projections have many uses, and the advantages and disadvantages of the fair-value and FCRA methods of making projections depend on how those projections are used. By placing a value on the financial risk absorbed by the government, fair-value estimates are particularly useful for evaluating changes in the amount of market risk that the government absorbs in federal credit programs. (Market risk is the component of financial risk that remains even after investors have diversified their portfolios as much as possible; it arises from shifts in macroeconomic conditions, such as productivity and employment, and from changes in expectations about future macroeconomic conditions.) Fair-value estimates are also useful for making comparisons between credit programs that have market risk and credit programs that do not—for example, between risky loans and up-front grants. However, if fair-value accounting is applied to some programs with market risk and not applied to others, comparisons between the former and the latter would be misleading.

Fair-value estimates may be less useful when policymakers are interested in the expected effects of legislation on future debt and deficits without regard to the value of the market risk that the government is absorbing. By not considering market risk and by simply discounting expected cash flows at Treasury-based rates, FCRA-based estimates of a program's costs align somewhat more closely with the program's cumulative cash flow effects than fair-value estimates do. Other disadvantages of fair-value estimates are that they can be more complicated to prepare than FCRA estimates are and inherently more uncertain if the prices of comparable securities cannot be readily observed. Finally, their meaning can be more difficult to communicate to lawmakers and the public.

CBO has written extensively about fair-value estimates for federal credit programs over the last several years in response to interest from the Congress.<sup>9</sup> Also, in accordance with rules introduced in recent House and Senate budget resolutions, the agency has produced not only FCRA-based estimates but also fair-value estimates of the costs of several credit programs. The fair-value estimates are generally higher than the FCRA-based estimates.

Most credit programs expose the government to market risk, because the government is most likely to incur large losses from its loans or loan guarantees when the economy is weak and borrowers are unable to repay their loans. Even when the government's ability to collect repayments from borrowers is relatively strong, as in the case of federal student loans, market risk is not completely eliminated. Furthermore, some features of federal credit programs—the income-based repayment provisions of federal student loans, for instance, or homeowners' ability to cancel their federally insured reverse mortgages in exchange for the value of the house—directly expose the government to market risk associated with fluctuations in aggregate income and prices.

9. For example, Congressional Budget Office, *Fair-Value Estimates of the Cost of Selected Federal Credit Programs for 2015 to 2024* (May 2014), [www.cbo.gov/publication/45383](http://www.cbo.gov/publication/45383), *Fair-Value Estimates of the Cost of Federal Credit Programs in 2013* (June 2012), [www.cbo.gov/publication/43352](http://www.cbo.gov/publication/43352), and letter to the Honorable Judd Gregg concerning CBO's analysis of the subsidy costs of direct and guaranteed student loans (July 27, 2009), [www.cbo.gov/publication/20774](http://www.cbo.gov/publication/20774).

Under FCRA, the costs of market risk are not included in estimates of the net value of federal credit programs reported in the budget. In contrast, market prices—which reflect market participants’ assessment of net value—are implicitly lowered by such costs. As a result, the acquisition of loans, loan guarantees, and other financial assets at or above market prices may appear under FCRA to make money for the government; conversely, sales of those items at or above market prices may appear under FCRA to result in losses. For example, financial assets that the government purchased at above-market prices under the Troubled Asset Relief Program would have appeared to create immediate budgetary savings if they had been accounted for under FCRA, rather than under the fair-value treatment required by legislation.

Not all of the government’s undertakings that have risk have significant market risk. In particular, risks related to some programs have no consistent relationship with changes in aggregate economic activity; that is, for those programs, the federal government has little exposure to market risk for a fair-value approach to account for. Consequently, fair-value estimates and FCRA estimates would be very similar.<sup>10</sup> For example, contracts for goods and services are subject to implementation risk—the risk that the vendor might not perform as required—which is unlikely to be related to economic conditions. Moreover, such contracts do not automatically obligate the government to make additional payments if a vendor underperforms. And for some programs, regardless of the significance of market risk, payments are limited to the amounts appropriated under current law.<sup>11</sup>

GAO’s report concluded that FCRA accounting was preferable to fair-value accounting. To support that conclusion, the report stated some drawbacks of fair-value accounting:

The introduction of market risk into subsidy costs under the fair value approach would (1) be inconsistent with long-standing federal budgeting practices primarily based on cash outlays; (2) be inconsistent with the budgetary treatment of similarly risky programs; (3) introduce transparency and verification issues with respect to inclusion of a noncash cost in budget totals; and (4) involve significant implementation issues, such as the need for additional agency resources.<sup>12</sup>

CBO has elsewhere discussed each of those drawbacks and potential remedies for some of them.<sup>13</sup> In CBO’s judgment, GAO puts more weight on consistency with cash-based accounting and verifiability of budget numbers than on estimates’ usefulness in making decisions. In practice, the Congressional budget process already makes a number of departures from narrow cash-based accounting, including the treatment of lease purchases and capital leases, the allocation of federal pension benefits in agencies’ budgets, and the treatment of federal interest costs. Some of those departures were introduced because the Congress decided

10. Neither a FCRA-based nor a fair-value estimate would match the cash-based estimate of such spending because of the effects of discounting.

11. In the case of federal credit programs, FCRA provides an automatic and indefinite appropriation for unexpected increases in program costs; a fair-value approach for those programs therefore measures the market value of the commitment under current law.

12. Government Accountability Office, *Credit Reform: Current Method to Estimate Credit Subsidy Costs Is More Appropriate for Budget Estimates Than a Fair Value Approach*, GAO-16-41 (January 2016), [www.gao.gov/products/GAO-16-41](http://www.gao.gov/products/GAO-16-41).

13. See, for example, testimony of Douglas W. Elmendorf, Congressional Budget Office, before the Committee on Financial Services, U.S. House of Representatives, *Testimony on Estimates of the Cost of the Credit Programs of the Export-Import Bank* (June 25, 2014), [www.cbo.gov/publication/45468](http://www.cbo.gov/publication/45468).

that cash-based estimates distorted decisions about how to allocate spending—which suggests that consistency with cash-based accounting has not been lawmakers' highest priority. FCRA itself is a departure from cash-based treatment, because it shifts the timing of cash flows and accounts for the time value of money by discounting.

GAO also states a more fundamental objection to fair-value accounting:

The additional market risk recognized under the fair value approach does not reflect additional cash costs beyond those already recognized by FCRA.

That objection assumes that the risky cash flows from a loan or loan guarantee can be adequately summarized by the average values from the projected distribution of possible outcomes. (Those averages are what GAO refers to as the cash cost.) Under FCRA, the averages are translated into a present value by being discounted at a rate that represents the government's borrowing cost. That approach essentially treats risky cash flows as having the same value as risk-free cash flows in the amount of the average of the risky cash flows, which is at odds with how such cash flows would be valued by the public.<sup>14</sup> In contrast, the fair-value approach uses the entire distribution of projected cash flows, and its relationship to the distribution of aggregate economic outcomes, to assess the cost of market risk.<sup>15</sup>

#### Senator Ayotte

**Question.** One of my biggest concerns is Congress' current inability to complete the budget process on time. Over the past 41 years, we have only completed the budget process on time 4 times—most recently in 1997—and we have had 173 short-term funding bills.

Since 1996, Congress has completed appropriations measures an average of 104 days after the start of the fiscal year.

In my home state of New Hampshire, we use a biennial budget process. With a national debt over \$19 trillion, it's time to bring New Hampshire common sense to how federal spending decisions are made.

In thinking about budget process reform, do you think it's more appropriate for us to compare biennial budgeting to short-term funding, rather than annual budgeting, since we so rarely complete the budgeting process?

14. For example, an equally likely chance of a future gain of \$20 in a strong economy or a future loss of \$10 in a weak economy would be treated as equivalent in value to a definite future gain of \$5. A private investor would put more weight on the bad aggregate outcome and value the risky cash flows at, say, \$3—less than the \$5 average of the projected cash flow outcomes.

15. For expositional purposes, that procedure is sometimes described as applying a higher discount rate—representing the source of the so-called noncash costs—to the same cash flows that would be expected under FCRA. However, a higher discount rate is not the core feature of fair-value accounting. The core feature is that the government values future cash flows in the same way that the public does, given the characteristics of those potential cash flows when administered by the government. For more discussion, see Congressional Budget Office, *Fair-Value Estimates of the Cost of Federal Credit Programs in 2013* (June 2012), [www.cbo.gov/publication/43352](http://www.cbo.gov/publication/43352).

What impact do stop-gap spending measures have on CBO's ability to assist Congress in carrying out its duties?

**Answer.** In thinking about alternatives to the current appropriation process, it is certainly useful to compare what would be expected to occur under a new approach with what actually occurs under the current system. In most recent years, regular appropriations have been enacted after the beginning of the fiscal year (sometimes several months later), following the enactment of one or more short-term continuing resolutions.<sup>16</sup> Partly to reduce the use of such temporary funding measures, some observers have proposed moving from an annual budget cycle to a biennial one. Biennial budgeting can take various forms: using a single measure to enact appropriations for two successive one-year periods, adopting a budget resolution for a two-year period, or providing funds that are made available for two years. Many proposals of biennial budgeting envision the enactment of all appropriations during one session of the Congress, reserving the other for oversight and other legislation.

Proponents of biennial budgeting contend that it could reduce the delay and repetition of the current budget process; establish more certainty in the process, thereby allowing executive branch agencies and recipients of federal funds to plan better and use resources more wisely; and free up time for other Congressional activities, such as oversight. Opponents argue that biennial budgets would be prepared too far in advance, requiring regular revisions because the underlying economic and budgetary forecasts would be less accurate and because circumstances would change; that biennial budgets could diminish oversight, because agencies' policies would be reviewed less frequently; and that more power might be shifted to the executive branch, because it might need more flexibility to make adjustments as time went on. Moreover, they argue that biennial budgeting would make it harder to challenge the status quo—because fundamental changes to programs need to be made incrementally, which would be more difficult in a two-year cycle.<sup>17</sup>

Stopgap spending measures have two effects on CBO's ability to assist the Congress in carrying out its duties. First, because stopgap spending measures usually cover the short term and are part of a larger process of adopting full-year appropriations, CBO analyzes more proposals and prepares more products during the annual appropriation process than it would otherwise have to. Although CBO has a well-defined process for preparing such products, they sometimes crowd out other work. Second, stopgap spending measures limit CBO's ability to plan effectively, particularly in its staffing decisions, and to use its resources efficiently.

**Question.** Last year, CBO indicated that responding to Congressional requests from both the majority and minority of multiple committees in both the Senate and the House was a continuing challenge.

Does this continue to be a challenge for CBO?

16. For further discussion, see James V. Saturno and Jessica Tollestrup, *Continuing Resolutions: Overview of Components and Recent Practices*, Report for Congress R42647 (Congressional Research Service, January 14, 2016).

17. To learn more, see Jessica Tollestrup, *Biennial Budgeting: Options, Issues, and Previous Congressional Action*, Report for Congress R41764 (Congressional Research Service, February 2, 2015).

How does CBO internally prioritize requests from Congress?

Is there a way for staff members to track the status of their CBO requests?

**Answer.** Yes, responding consistently in a balanced, timely, and analytically sound way, given the ebbs and flows of legislative activity, is sometimes a challenge. That challenge can arise, for instance, when major legislation is being considered and Members of both the majority and minority, sometimes in both the House and Senate, are seeking estimates of multiple variants or amendments. (Examples of major legislation include major farm bills, highway funding, the defense authorization bill, and legislation reauthorizing a major program.) Also, the Congress continues to be acutely interested in analyses of the Affordable Care Act (ACA) and of numerous proposals for further changes in federal health care programs; such analyses can be very complicated and time-consuming. The challenge can also arise when multiple appropriation bills are being considered in a short period, when a committee has ordered reported many bills in a particular subject area, when legislative priorities suddenly change, or when significant legislative action coincides with CBO's preparation of its baseline projections or other major products that are necessary for the budget process.

In general, CBO's work follows processes and priorities specified in the Congressional Budget and Impoundment Control Act of 1974 and subsequent laws or developed by the agency in concert with the budget committees and the Congressional leadership. CBO's chief responsibility under the Budget Act is to help the budget committees with the matters under their jurisdiction. CBO also supports other Congressional committees—particularly the Appropriations, Ways and Means, and Finance Committees, as the Budget Act requires—and the Congressional leadership.

CBO regularly consults with committees and the Congressional leadership to ensure that its resources are focused on the work that is of highest priority to the Congress. The agency coordinates with committees to determine when they plan to file bill reports and aims to complete cost estimates in time to be included in those reports. When a committee approves many bills simultaneously, or when multiple committees are considering legislation in the same subject area, CBO determines the priority of its work on cost estimates—in consultation with the committees—according to committees' plans for issuing reports and plans for when the bills will be considered by the Senate or House as a whole. Because the pace of Congressional action often requires CBO to produce its analysis quickly, the amount of explanation that can be provided with an estimate or analytic report is usually limited by the time available. How to strike the appropriate balance among publishing additional explanation, undertaking new analyses, and pursuing other responsibilities is part of the guidance about priorities that CBO seeks from committees and the Congressional leadership.

If staff members have been in touch with CBO about a cost estimate and want to inquire about its status, they should feel free to contact the CBO analyst with whom they have been working. They may also direct inquiries to CBO's Budget Analysis Division by emailing [costestimates@cbo.gov](mailto:costestimates@cbo.gov) or by calling (202) 226-2800. For other inquiries, they may send email to [congressionalaffairs@cbo.gov](mailto:congressionalaffairs@cbo.gov) or call (202) 226-2700.

**Question.** According to CBO, federal spending is expected to grow by 60 percent over the next 10 years. In addition, net interest costs are projected to rise sharply—and that projection is based on low interest rates.



Since its January projection, CBO has reduced the projections of interest rate growth, reflecting lower economic growth and continued demand for Treasury securities.

If interest rates were 1 percentage point higher per year than in your baseline, what would that do to the baseline projected deficit over the period from 2017 through 2041?

What do you see as the biggest risk that could cause our long-term debt situation to turn out worse than in the baseline scenario?

**Answer.** CBO has previously analyzed the scenario in which interest rates on federal debt held by the public are 1 percentage point higher per year than they are projected to be in its extended baseline projection.<sup>18</sup> In that scenario, debt and deficits over the 2017–2041 period are higher than they are in the extended baseline. Debt in 2041 is projected to equal 158 percent of GDP in that scenario, 33 percentage points higher than in the extended baseline.<sup>19</sup>

CBO has not identified a single largest risk in the outlook for federal debt. Developments that could make it much larger than it is in CBO's projections include higher interest rates; lower productivity growth; higher spending per beneficiary in Medicare and Medicaid; a severe economic recession; and catastrophes, such as a major natural disaster or world war.

**Question.** Spending for Social Security, the major health care programs—Medicare, Medicaid, the Children's Health Insurance Program, and subsidies for health insurance purchased through exchanges created by the Affordable Care Act—and net interest on our national debt together account for nearly 85 percent of the total increase in outlays over the next decade.

Would it be possible to put our country on a fiscally sustainable path without reforming our safety-net programs?

**Answer.** In its most recent baseline projections, CBO projected that deficits under current law would rise to 86 percent of GDP by 2026, a little more than twice the average over the past five decades. In later years, debt would rise even more sharply, reaching 155 percent of GDP three decades from now, a higher percentage than any previously recorded in the United States.

Anticipated growth in spending for Social Security and the major health care programs contributes significantly to those projections. By 2026, if current law did not change, CBO projects that spending for Social Security and the major health care programs would account for almost two-thirds of all federal noninterest spending. Therefore, substantially lowering federal deficits and debt without reducing spending on those programs would require large decreases in other noninterest spending, large increases in revenues, or both.

18. See Congressional Budget Office, *The 2016 Long-Term Budget Outlook* (July 2016), [www.cbo.gov/publication/51580](http://www.cbo.gov/publication/51580).

19. See Congressional Budget Office, "Long-Term Budget Projections" (July 2016), [www.cbo.gov/about/products/budget\\_economic\\_data#1](http://www.cbo.gov/about/products/budget_economic_data#1).

CBO has periodically published analyses of specific policy options that would reduce deficits, including options that would reduce spending on Social Security and health care.<sup>20</sup> Those options indicate how changes could be spread broadly across all parts of the budget and how the changes would need to be proportionately larger if they were concentrated in certain parts of the budget.

CBO has recently analyzed several long-term scenarios that illustrate the effects of deficit-reducing policies.<sup>21</sup> For example, for debt in 2046 to equal 75 percent of GDP (its current percentage), lawmakers would need to make the federal deficit smaller than the baseline deficit by an amount averaging 1.7 percent of GDP per year, CBO estimates. (In 2017, that would be about \$330 billion, or \$1,000 per person, and the dollar amount would grow as time went on.) If lawmakers achieved that deficit reduction only by boosting revenues, total revenues would have to be 9 percent higher per year than they are in CBO's extended baseline. If they achieved it only by cutting noninterest spending, that spending would have to be reduced by 8 percent. If such a spending reduction excluded Social Security and the major health care programs, other noninterest spending would have to be reduced by 24 percent.

#### Senator Crapo

**Question.** Dr. Hall, I have a few questions with regard to how CBO incorporates the spending and revenue effects of executive agency regulations in its baseline.

At what point in the regulatory process does CBO consider a regulation, proposed regulation or other executive action to be "current law," and thus have its outlay and/or revenue effects incorporated into your current law baseline?

**Answer.** In preparing baselines and cost estimates, CBO makes its best judgment about what major actions by the Administration are likely to occur. When making that judgment, CBO takes various factors into account, including current law, public statements and documents, information accompanying the President's budget proposals, previous actions by the Administration, informal communication with staff members of executive branch agencies, and the nature of the considerations that are likely to bear on the Administration's decisions.

If it is clear under current law when an action will be implemented and what precisely that action will be, CBO incorporates the budgetary effect of that action into the baseline. In contrast, if it appears unlikely that an action will take place (or that it will have any significant budgetary effect), CBO does not incorporate its budgetary effect into the baseline.

In some cases—for example, when proposed rules are issued—it is unclear whether there will be an action or what precisely it will be. In such cases, CBO assigns a 50 percent probability to the action outlined in the proposed rule, even though the final rule may wind up implementing a different action. That probability reflects both the likelihood that

20. For example, see Congressional Budget Office, *Options for Reducing the Deficit: 2015 to 2024* (November 2014), [www.cbo.gov/budget-options/2014](http://www.cbo.gov/budget-options/2014), and *Choices for Deficit Reduction: An Update* (December 2013), [www.cbo.gov/publication/44967](http://www.cbo.gov/publication/44967).

21. See Congressional Budget Office, *The 2016 Long-Term Budget Outlook* (July 2016), Chapter 1, [www.cbo.gov/publication/51580](http://www.cbo.gov/publication/51580).

the action will be taken and the likelihood that it will have the full potential effect. In other words, the adjustment is equivalent to assuming that an action will occur and that it will have half the maximum possible effect; it is also equivalent to assuming that there is a 50 percent chance that an action having the full effect will take place and a 50 percent chance that either no action will take place or the action will have no budgetary effect. When CBO assigns a 50 percent probability to an action, half of its potential cost or savings is incorporated into the baseline. CBO may also have to make an assumption about the timing of such an action.

Once a final action is taken—for instance, once a final regulation is issued—that final action becomes the basis for CBO's cost estimates of legislation, regardless of what was originally assumed for the baseline projections. That is, when CBO estimates the effects of legislation, it uses a baseline that has been adjusted to reflect new administrative actions. And those administrative actions are automatically included in the baseline the next time it is updated.

That practice of incorporating the effects of specific rules and regulations into the baseline applies mostly to large, easily identifiable actions that differ from the expectations that CBO has incorporated into the baseline. The Administration takes thousands of smaller regulatory and administrative actions each year that are not specifically taken into account in the baseline. However, an agency's costs of implementing those actions are included in CBO's budgetary projections for that agency.

**Question.** Does CBO publish either a running tally or an annual report showing the total annual revenue and outlay effects of all annual agency regulations and executive actions that are considered by CBO to be current law, net of any revenue and outlay effects that had already been incorporated in the baseline at the time any legislation that may have authorized any of those regulations or executive actions was enacted?

**Answer.** No, CBO does not track or estimate the costs of implementing regulations or other executive actions in the same way that it estimates the costs of legislative changes that are enacted into law. In most cases, the budgetary effects of particular regulations and executive actions cannot be separately identified among the effects of the many thousands that are or will be in effect. Instead, those effects are usually incorporated into CBO's projections of spending from agencies' overall operating accounts, from particular program accounts, or from broad sources of revenues. CBO therefore has no basis for comparing the budgetary effects of current regulations and executive actions with those that were already in effect when the underlying laws were enacted.

**Question.** If not, could you please provide the committee with those net revenue and outlay numbers, as described in Question #2, for either the most recent fiscal or calendar year?

**Answer.** Please see the answer to the previous question.

**Question.** During the September 7, 2016, House Budget Committee hearing entitled "Center for Medicare and Medicaid Innovation: Scoring Assumptions and Real-World Implications," Chairman Price expressed concerns with the opaque nature of CBO's cost estimates associated with demonstrations run through CMMI. CBO initially estimated that CMMI would yield \$1.3 billion in savings by 2019. In July 2015, CBO assumed \$27 billion

in savings over 10 years due to CMMI demonstrations. During the House Budget hearing, CBO Deputy Director Mark Hadley testified that the innovation center will now save an estimated \$34 billion over the next 10 years. CBO maintains that it does not know which, if any, of the current demonstrations will result in savings, yet CBO claims that altering any of CMMI's demonstration activities would result in a substantial loss in those savings. This practice makes it almost cost prohibitive for Congress to alter CMMI policy or conduct appropriate oversight, which is particularly concerning given the scope and scale of the proposed Medicare Part B drug payment model.

Which specific CMMI actions or demonstrations prompted CBO to increase its cost savings estimate from \$27 billion in 2015 to \$34 billion in 2016?

**Answer.** CBO's current estimate indicates that CMMI's activities will reduce federal spending by \$34 billion from 2017 through 2026. That estimate is higher than the corresponding 10-year estimate of \$27 billion provided in the agency's 2015 blog post, mostly because the earlier estimate was for a slightly earlier time period (2016 through 2025).<sup>22</sup> Compared with the estimate in CBO's blog post, the calculations for the agency's current estimate excluded a year (2016) with estimated federal savings of less than \$500 million and added a year (2026) with estimated federal savings of \$7 billion. Estimated savings are relatively low in 2016 because CMMI is still in its early stages of development and higher in 2026 because more demonstrations will be completed by that time. The two estimates do not differ because of any specific actions by CMMI or the results of any particular demonstrations.

**Question.** How has CBO's scoring methodology for CMMI changed to incorporate and reflect the actual influence of demonstrations on the delivery of health care?

**Answer.** CBO has not modified its scoring methodology or its budget projections for CMMI's activities on the basis of the center's experiences with demonstrations to date. CBO is actively monitoring the demonstrations being conducted by CMMI but does not believe that the information gathered thus far provides a basis for assessing the accuracy of the agency's budget projections. Evaluation reports are not yet available for many demonstrations, and results from those that are available reflect only the early experiences of some demonstrations. Those initial results are not generally sufficient for drawing conclusions about the likely success of the models being tested.

Over the next several years, CBO expects to learn much more about CMMI's activities and will use that information to improve its budget projections. CBO will continue monitoring all aspects of CMMI's activities, including its approach to selecting, testing, and evaluating demonstrations. CBO will pay particular attention to evaluation reports that are released and decisions by HHS about whether or not to expand some demonstrations—and to the projected savings from those that are expanded.

**Question.** During the House Budget Committee hearing, Mr. Hadley indicated that the pending CMMI Part B Drug Payment Model is more difficult for CBO to assess because it is

22. Congressional Budget Office, "Estimating the Budgetary Effects of Legislation Involving the Center for Medicare & Medicaid Innovation," *CBO Blog* (July 30, 2015), [www.cbo.gov/publication/50692](http://www.cbo.gov/publication/50692).

“very large relative to the size of some other demonstrations” and the parameters were “only announced in a notice of proposed rulemaking, so we don’t know what the final parameters of the program will look like ...” In your opinion, does that illustrate a fundamental challenge with CMMI and CBO cost estimates—that CBO simply cannot provide Congress the predictability it needs?

**Answer.** When asked to estimate the cost of a legislative proposal, CBO seeks to provide the Congress with the most accurate estimate possible. To achieve that goal, CBO reviews available research and other relevant information and engages in discussions with experts in the field. Some estimates are more challenging to develop than others. CBO’s recent cost estimate for H.R. 5122, which would prevent the Secretary of Health and Human Services from implementing a proposed demonstration to modify the payment method for prescription drugs covered under Medicare Part B, was challenging because the proposed demonstration is very large and because the parameters of the demonstration were announced in a notice of proposed rulemaking and, therefore, might change substantially.<sup>23</sup> (To estimate the cost of the bill to prevent the demonstration, CBO first assessed how the demonstration would affect federal spending. The effect of blocking the demonstration is the reverse of that estimate, offset in part by the expectation that CMMI would pursue alternative demonstrations that have the potential to achieve savings.)

CBO acknowledged that its cost estimate for that bill reflects considerable uncertainty, largely because the details of the demonstration have not been finalized. Past experience indicates that policy changes in final rules are often much smaller than those in the corresponding proposed rules. To account for that, CBO estimated that the savings from the demonstration as implemented under the final rule would be one-half the savings estimated on the basis of the parameters in the proposed rule.

#### Senator Johnson

**Question.** What is the soonest you can provide a report detailing the changes in direct spending and revenue associated with the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (hereafter referred to as “Affordable Care Act”), including the net impact on deficit, both with on-budget and off-budget effects? The information requested would be similar to that provided in Table 2 of CBO’s March 20, 2010 estimate of the budgetary effects of the Affordable Care Act, as passed by the Senate.

23. See Congressional Budget Office, cost estimate for H.R. 5122, a bill to prohibit further action on the proposed rule regarding testing of Medicare Part B prescription drug models (October 4, 2016), [www.cbo.gov/publication/52087](http://www.cbo.gov/publication/52087).

**Answer.** CBO and the staff of the Joint Committee on Taxation (JCT) cannot readily provide a retrospective analysis of the Affordable Care Act that is analogous to the cost estimate provided by the agencies in 2010.<sup>24</sup> The two main reasons are the following:<sup>25</sup>

- The incremental budgetary effects of many provisions of the ACA are embedded in CBO's baseline projections for preexisting programs and tax revenues, and they cannot be separately identified by means of the agencies' normal estimating procedures—which are generally based on data that reflect all of the provisions of current law, including the ACA.<sup>26</sup>
- A retrospective analysis of the effects of a current law is very different from a cost estimate for proposed legislation, particularly because it requires formulation of a counterfactual benchmark representing what would have happened if the law had not been enacted—a challenging undertaking that is beyond the scope of CBO's usual analyses. In this case, such a counterfactual benchmark would include, for example, guesses of what Medicare's rules and payment rates would have been in the absence of the ACA, as well as guesses of how taxpayers would have organized their financial affairs. Given the number and complexity of the changes to Medicare under the ACA, creating a counterfactual benchmark would be a very complicated task that would take months of work, and the resulting benchmark would be hugely uncertain and speculative. (Those constraints are not unique to the ACA; they apply to most legislation that affects preexisting federal programs. For that reason, CBO has traditionally not produced retrospective estimates of the budgetary effects of enacted legislation.)

CBO and JCT have revised their estimated budgetary effects of some aspects of the ACA. But those revisions give the agencies no reason to think that their initial assessment—that the ACA would reduce budget deficits—was incorrect.

CBO and JCT can continue to estimate the effects of *prospective* legislative actions, such as proposals to modify provisions of the ACA or to repeal the law entirely. Because of the

24. See Congressional Budget Office, cost estimate for H.R. 4872, the Reconciliation Act of 2010 (Final Health Care Legislation) (March 20, 2010), [www.cbo.gov/publication/21351](http://www.cbo.gov/publication/21351). The letter that reported that cost estimate showed projections of the effects of enacting both the Patient Protection and Affordable Care Act (PPACA) as passed by the Senate (H.R. 3590) and the Health Care and Education Reconciliation Act of 2010 (H.R. 4872). The latter included provisions related to education. CBO uses the term "Affordable Care Act" to refer to PPACA (Public Law 111-148); the health care provisions of the Reconciliation Act (P.L. 111-152); and the effects of subsequent judicial decisions, statutory changes, and administrative actions. For JCT's estimates of the effects of most of the tax provisions in the ACA, see Joint Committee on Taxation, *Estimated Revenue Effects of the Amendment in the Nature of a Substitute to H.R. 4872, the "Reconciliation Act of 2010," in Combination With the Revenue Effects of H.R. 3590, the "Patient Protection and Affordable Care Act (PPACA)," as Passed by the Senate, and Scheduled for Consideration by the House Committee on Rules on March 20, 2010*, JCX-17-10 (March 20, 2010), <http://go.usa.gov/8tNQ>.

25. For more information on why it is not possible to produce a new estimate for the ACA, see Congressional Budget Office, *Answers to Questions for the Record Following a Hearing on the Budget and Economic Outlook for 2014 to 2024 Conducted by the Senate Committee on the Budget* (June 10, 2014), pp. 15–18, [www.cbo.gov/publication/45396](http://www.cbo.gov/publication/45396).

26. CBO made this point shortly after the enactment of the ACA, when the agency first incorporated that legislation into its baseline projections. See *The Budget and Economic Outlook: An Update* (August 2010), pp. 6–7, [www.cbo.gov/publication/21670](http://www.cbo.gov/publication/21670). See also Congressional Budget Office, *Updated Estimates of the Effects of the Insurance Coverage Provisions of the Affordable Care Act, April 2014* (April 2014), p. 1, [www.cbo.gov/publication/45231](http://www.cbo.gov/publication/45231).

complexities involved in implementing a repeal of the ACA and changes induced by the ACA that would be sustained even if the law was repealed, the budgetary effects of repealing the act would not simply be the opposite of the budgetary effects of the ACA itself. Last year, CBO estimated that repealing the ACA would increase deficits by \$137 billion over the 2016–2025 period.<sup>27</sup>

**Question.** You testified that CBO has altered its projections regarding the Affordable Care Act's marketplace since the law was passed in 2010. As you noted, enrollment in the marketplace has been lower than originally projected.

With respect to subsidies through the marketplace:

- (a) What is the average subsidy per person for each fiscal year and calendar year that the marketplace has been in place and what do you project it will be in each fiscal year and calendar year over the ten-year budget window?
- (b) How many subsidized enrollees were there in each fiscal year and calendar year and how many subsidized enrollees do you project there will be in each fiscal year and calendar year over the ten-year budget window?
- (c) What was the total cost of marketplace subsidies in each fiscal year and calendar year so far and what do you project it will be in each fiscal year and calendar year over the ten-year budget window?
- (d) How does the average subsidy per person, the number of subsidized enrollees, and the total cost of subsidies compare to CBO's earlier estimates for the same fiscal and calendar years?
- (e) How will recent premium increases and reduced insurer participation affect CBO's cost and coverage projections for the Affordable Care Act in the next baseline?

**Answer.** CBO and JCT model insurance coverage on a calendar year basis, because many insurance plans are provided for calendar years and because data are typically available on a calendar year basis. But the agencies model the budgetary effects of insurance coverage on a fiscal year basis, because that is how subsidies for that coverage are recorded in the budget. As a result, some of the following answers use calendar years and some fiscal years, according to the information that is available in the agencies' projections.

(a) CBO and JCT cannot precisely determine the average subsidy per subsidized enrollee in the health insurance marketplaces or the Basic Health Program during 2014 or 2015, because that calculation would require information about the reconciliation of the premium tax credits and cost-sharing subsidies that is not yet publicly available. But the agencies estimate that the average subsidy was about \$3,700 for calendar year 2014 and about \$4,100 for the following year.

In August 2016, CBO and JCT projected that the average subsidy per subsidized enrollee in the health insurance marketplaces or the Basic Health Program would be \$4,420 in calendar

27. See Congressional Budget Office, *Budgetary and Economic Effects of Repealing the Affordable Care Act* (June 2015), [www.cbo.gov/publication/50252](http://www.cbo.gov/publication/50252).

year 2016. For years after 2016, the agencies have not updated their projections of that average since last March, when they projected that it would be \$4,550 in 2017 and \$7,110 in 2026.<sup>28</sup>

(b) CBO and JCT estimate that 5 million people, on average, were enrolled in subsidized coverage through the health insurance marketplaces during calendar year 2014 and that 8 million people were in 2015. In August 2016, CBO and JCT projected that there would be an average of 9 million people enrolled in subsidized coverage through the marketplaces during calendar year 2016. The agencies currently project that the average will be 12 million in calendar year 2017, 15 million in 2018, 16 million in 2019, 15 million in each year from 2020 to 2024, and 14 million in 2025 and 2026.<sup>29</sup>

(c) Because the marketplace subsidies are structured as refundable tax credits, some of their cost takes the form of increased outlays (to the extent that the credits exceed enrollees' income tax liability); the remainder takes the form of lower tax revenues. Total outlays for marketplace subsidies were \$13 billion in fiscal year 2014 and \$27 billion in fiscal year 2015, but those totals do not include the portion of premium tax credits that are classified as a reduction in revenues. CBO and JCT estimate that those revenue reductions represent about 10 percent to 15 percent of the total subsidy in each year.

CBO and JCT estimated in August 2016 that the total cost of marketplace subsidies, including the portion of premium tax credits that is classified as a reduction in revenues, will be \$37 billion in fiscal year 2016, \$51 billion in 2017, \$68 billion in 2018, \$77 billion in 2019, \$83 billion in 2020, \$87 billion in 2021, \$91 billion in 2022, \$95 billion in 2023, \$98 billion in 2024, \$103 billion in 2025, and \$107 billion in 2026.

(d) CBO and JCT's most recent estimate (in August 2016) of the average subsidy per subsidized enrollee in calendar year 2016 was \$4,420. The same estimate—that is, for calendar year 2016—was \$4,240 in March 2016, \$4,040 in March 2015, \$4,830 in April 2014, \$5,350 in May 2013, and \$5,300 in the original estimate for the ACA in 2010.

The agencies' current estimate of the total number of subsidized enrollees in the marketplaces is 9 million for calendar year 2016. The same estimate was 10 million in March 2016, 15 million in March 2015, 19 million in April 2014, 19 million in May 2013, and 17 million in 2010.

The agencies currently project that the total cost of marketplace subsidies in fiscal year 2016 will be \$37 billion. The same estimate was \$42 billion in March 2016, \$52 billion in March 2015, \$74 billion in April 2014, \$87 billion in May 2013, and \$77 billion in 2010.

(e) CBO's next major update to its baseline projections will incorporate available data about premiums for insurance in the marketplaces, enrollment in the marketplaces, and insurers' participation in the marketplaces. Among the data that will be incorporated are final data about premiums for 2017 coverage—which only recently became available and that appear to show somewhat higher premiums than CBO and JCT had anticipated.

28. For those projections, as well as projections for each of the intervening years, see Congressional Budget Office, *Federal Subsidies for Health Insurance Coverage for People Under Age 65: 2016 to 2026* (March 2016), Table 4, [www.cbo.gov/publication/51385](http://www.cbo.gov/publication/51385).

29. *Ibid.*, Table 1.



**Question.** How do the characteristics (e.g., age, income, health status, etc.) of enrollees in the marketplaces so far compare with what CBO originally expected? Has CBO updated its estimates to account for any discrepancies?

**Answer.** CBO and JCT regularly make adjustments to their estimates of marketplace enrollment, using newly available information about the number of enrollees and their characteristics, and the agencies will continue to do so in the future. So far, those enrollees have been somewhat older, on average, than CBO and JCT initially anticipated. The share of total enrollees with subsidies is also higher than the agencies originally estimated.

**Senator Stabenow**

**Question.** In the oversight hearing last year, I asked you to address concerns about the accuracy and impartiality of dynamic scoring given the large number of assumptions that have to be made. You noted that there is uncertainty in any estimate, but that you expected including macroeconomic effects would improve estimates for complex legislation. Additionally, you said that CBO constantly scrutinizes errors and reviews estimates to make future improvements. Having now been at CBO for over a year, can you comment on any unexpected challenges with dynamic scoring? Has CBO conducted new analysis of previous estimates?

**Answer.** Since you asked about these issues last year, CBO has published five cost estimates that incorporated macroeconomic feedback (a process often called “dynamic scoring”). Three of those five were cost estimates of the Restoring Americans’ Healthcare Freedom Reconciliation Act of 2015, H.R. 3762. The analysis underlying them was conducted jointly by CBO and the staff of the Joint Committee on Taxation. The remaining two were cost estimates of revenue legislation for which the analysis was conducted by JCT.

In an earlier report, CBO anticipated and discussed the challenges that would later be posed by the three estimates of H.R. 3762.<sup>30</sup> Above all, estimates of the macroeconomic effects of repealing the Affordable Care Act are very uncertain, largely because the law’s effects on labor markets are themselves uncertain. That uncertainty, in turn, arises partly because many of the ACA’s provisions have been in place for less than two years and partly because estimates of how workers and businesses might respond to the law vary considerably.

CBO has not performed new analyses of previous dynamic cost estimates. Because H.R. 3762 has not been enacted, the agency cannot observe outcomes under its provisions and therefore cannot compare those outcomes to its dynamic cost estimate.

**Question.** The macroeconomic effects for many programs, assuming they could be accurately estimated, fall outside of the 10-year budget window. Has CBO looked at the accuracy of dynamic scoring for estimations outside of the 10-year window?

30. Congressional Budget Office, *Budgetary and Economic Effects of Repealing the Affordable Care Act* (June 2015), [www.cbo.gov/publication/50252](http://www.cbo.gov/publication/50252).

**Answer.** When preparing a cost estimate of major legislation and when that cost estimate incorporates macroeconomic feedback, CBO and JCT are required to provide a qualitative assessment of the budgetary effects of the legislation over a 30-year period. Also, CBO sometimes extends its dynamic analysis of illustrative policies beyond the normal 10-year horizon, recognizing that macroeconomic feedback to the budget can be important in the long term. For example, in its most recent report about the long-term budget outlook, CBO shows how different assumptions about federal deficits would affect the economy and quantifies how feedback from those economic effects in turn would affect the budget in the long term.<sup>31</sup>

In analyzing major legislation, accounting for the feedback to the budget increases the accuracy of analyses that extend beyond the 10-year window, because that feedback generally grows larger and larger over time, in CBO's view. Nonetheless, such analyses are subject to enormous uncertainty. For example, in circumstances in which CBO has quantified ranges of likely possible outcomes, those ranges have grown wider as the analysis extends farther into the future.<sup>32</sup>

Determining the accuracy of CBO's cost estimates after the fact is often quite difficult and sometimes impossible, whether the estimates are conventional or dynamic. Even several years after a policy is enacted, it is often difficult to disentangle its direct impact on the budget from the impact of unrelated changes. Similarly, the macroeconomic feedback resulting from a particular law may contribute only a small part of the law's overall effect on the budget, and it usually cannot be identified separately after the fact. Those problems grow larger the farther one moves beyond the 10-year window.

**Question.** Data from other government agencies and outside groups suggests that shutdowns, near-breaches of the debt ceiling, and continuing resolutions have a real cost to families, businesses, and taxpayers. For example, in 2011, debt ceiling brinksmanship led to the first ever downgrade in the Standard & Poor's credit rating of long-term federal debt. The delay in raising the limit led to a \$1.3 billion increase in the Treasury's borrowing costs, and according to the Bipartisan Policy Center, the political showdown cost taxpayers \$18.9 billion over 10 years. According to Standard & Poor's, the 2013 shutdown led to \$24 billion in lost economic growth. Has CBO calculated the cost of shutdowns, continuing resolutions, and near breaches of the debt ceiling? Should this cost be incorporated into our budget process in some way?

**Answer.** CBO has not explicitly calculated the costs of shutdowns, continuing resolutions, and near breaches of the debt ceiling. However, the Congressional Research Service (CRS) and the Government Accountability Office have both produced useful material about

31. See Congressional Budget Office, *The 2016 Long-Term Budget Outlook* (July 2016), Chapter 6, [www.cbo.gov/publication/51580](http://www.cbo.gov/publication/51580).

32. See Congressional Budget Office, *Budgetary and Economic Outcomes Under Paths for Federal Revenues and Noninterest Spending Specified by Chairman Price, March 2016* (March 2016), [www.cbo.gov/publication/51260](http://www.cbo.gov/publication/51260).

government shutdowns.<sup>33</sup> For instance, CRS issued a report in 2015 about studies of the October 2013 shutdown.<sup>34</sup> The report found that although economic forecasters identified some small direct losses of economic activity during the shutdown, which lasted for two and a half weeks, much of that loss was subsequently recouped, so the overall costs to the economy were minimal. A longer shutdown would probably increase the amount of direct economic loss that could not be recouped.

It is much harder to estimate the indirect loss of economic output that might stem from heightened uncertainty related to the occurrence or possibility of a government shutdown. In general, households' and businesses' uncertainty about fiscal and regulatory policies tends to dampen economic output. However, quantifying that uncertainty and identifying its sources is difficult. Possible sources of recent uncertainty include disagreement among policymakers about whether to extend certain key provisions governing fiscal policy, the debate about how to put debt on a sustainable path, the protracted debate about rules for implementing major legislation in the health care and financial sectors, possible changes in rules related to energy and the environment, and the unpredictability of the appropriations process. Uncertainty from those and other sources has probably dampened growth, but CBO has not estimated how much.

When CBO develops the economic forecast that underlies its baseline projections, it does implicitly incorporate the effects of particular events that have occurred and the effects of uncertainty about future events. For example, if a shutdown occurred, to the degree that it resulted in a permanent loss of national income, that effect would be incorporated into CBO's assessment of the economy, and the agency's baseline projections of revenues would consequently be lower.

But the federal budget process is generally geared to measuring the effects of Congressional action rather than of inaction. If the process were different—if in the absence of appropriations, for instance, discretionary funding were automatically maintained at the levels specified in continuing resolutions—the effects of legislation that would cause a shutdown would be considered in the budget process, because that legislation would represent a departure from current law. Such a change in the appropriation process would essentially convert trillions of dollars of future discretionary spending into mandatory spending.

33. For a list of CRS's reports and of documents on the same topic from other sources, see Jared C. Nagel and Justin Murray, *Past Government Shutdowns: Key Resources*, Report for Congress R41759 (Congressional Research Service, September 15, 2015). For GAO's report on the economic effects of the October 2013 shutdown, see Government Accountability Office, *2013 Government Shutdown: Three Departments Reported Varying Degrees of Impacts on Operations, Grants, and Contracts*, GAO-15-86 (October 2014), [www.gao.gov/products/GAO-15-86](http://www.gao.gov/products/GAO-15-86).

34. Marc Labonte, *The FY2014 Government Shutdown: Economic Effects*, Report for Congress R43292 (Congressional Research Service, September 11, 2015).